No. 17-130	
Title:	**Raymond J. Lucia, et al., Petitioners** **v.** **Securities and Exchange Commission**
Docketed:	July 26, 2017
Lower Ct:	United States Court of Appeals for the District of Columbia Circuit
Case Numbers:	(15-1345)
Decision Date:	June 26, 2017
Questions Presented	

DATE	PROCEEDINGS AND ORDERS
Jul 21 2017	Petition for a writ of certiorari filed. (Response due August 25, 2017)
Jul 28 2017	Blanket Consent filed by Petitioners, Raymond J. Lucia, et al. on 07/31/2017
Aug 16 2017	Order extending time to file response to petition to and including September 25, 2017.
Aug 25 2017	Brief amicus curiae of The Chamber of Commerce of the United States filed.
Aug 25 2017	Brief amicus curiae of Pacific Legal Foundation filed.
Aug 25 2017	Brief amicus curiae of Mark Cuban filed.
Aug 25 2017	Brief amicus curiae of Cato Institute filed.
Sep 14 2017	Order further extending time to file response to petition to and including October 25, 2017.
Sep 19 2017	Brief amicus curiae of Anthony Michael Sabino filed.
Oct 17 2017	Letter of October 17, 2017 from counsel for petitioners received.
Oct 18 2017	Order further extending time to file response to petition to and including November 15, 2017.

Nov 14 2017	Motion to extend the time to file a response from November 15, 2017 to November 29, 2017, submitted to The Clerk. **Main Document**
Nov 14 2017	Order further extending time to file response to petition to and including November 29, 2017.
Nov 29 2017	Brief of respondent Securities and Exchange Commission filed. **Proof of Service** **Main Document**
Dec 13 2017	DISTRIBUTED for Conference of 1/5/2018.
Dec 13 2017	Reply of petitioners Raymond J. Lucia, et al. filed. (Distributed) **Main Document** **Proof of Service** **Certificate of Word Count**
Jan 08 2018	DISTRIBUTED for Conference of 1/12/2018.
Jan 12 2018	Petition GRANTED.
Jan 16 2018	Blanket Consent filed by Petitioners, Raymond J. Lucia, et al.. **Blanket Consent**
Jan 18 2018	Anton Metlitsky, Esquire, of New York, New York, is invited to brief and argue this case, as amicus curiae, in support of the judgment below.
Jan 26 2018	Letter of petitioners Raymond J. Lucia, et al. on behalf of the parties filed. **Main Document**
Feb 07 2018	The joint appendix, petitioners' brief on the merits, and brief of respondent Securities and Exchange Commission shall be filed on or before February 21, 2018. Any amicus curiae briefs in support of petitioners or in support of neither party shall be filed on or before February 28, 2018.
Feb 07 2018	The brief of Court-Appointed amicus curiae in support of the judgment below shall be filed on or before March 26, 2018. Any other amicus curiae brief supporting affirmance (the judgment below) shall be filed on or before April 2, 2018.
Feb 07 2018	Blanket Consent filed by Respondent, Securities and Exchange Commission **Blanket Consent**
Feb 08 2018	Motion to dispense with printing the joint appendix filed by petitioners Raymond J. Lucia, et al. **Main Document** **Proof of Service**

Feb 20 2018	Motion to dispense with printing the joint appendix filed by petitioners GRANTED.
Feb 21 2018	Brief of petitioners Raymond J. Lucia, et al. filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 21 2018	Brief of respondent Securities and Exchange Commission in support of petitioners filed. **Main Document** **Proof of Service**
Feb 21 2018	Brief amicus curiae of Cato Institute filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 22 2018	Brief amicus curiae of Anthony Michael Sabino filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 23 2018	SET FOR ARGUMENT on Monday, April 23, 2018.
Feb 23 2018	Brief amicus curiae of SHOW, Inc. filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 26 2018	Brief amicus curiae of Federal Administrative Law Judges Conference in support of neither party filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 27 2018	Brief amicus curiae of Pacific Legal Foundation filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 27 2018	Brief amicus curiae of The Forum of United States Administrative Law Judges in support of neither party filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 28 2018	Brief amicus curiae of Washington Legal Foundation filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 28 2018	Brief amicus curiae of The Chamber of Commerce of the United States filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 28 2018	Brief amici curiae of Administrative Law Scholars in support of neither party filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 28 2018	Brief amici curiae of States of Utah, et al. filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Feb 28 2018	Brief amicus curiae of Professor Jennifer L. Mascott filed.

	Main Document Count	**Certificate of Word Count**	**Certificate of Word**
Feb 28 2018	Brief amici curiae of RD Legal Capital, LLC and Roni Dersovitz filed.		
	Main Document	**Certificate of Word Count**	**Proof of Service**
Feb 28 2018	Brief amici curiae of J.S. Oliver Capital Management, L.P. and Ian O. Mausner filed.		
	Main Document	**Certificate of Word Count**	**Proof of Service**
Feb 28 2018	Brief amici curiae of Urska Velikonja and Joseph A. Grundfest in support of neither party filed.		
	Main Document	**Certificate of Word Count**	**Proof of Service**
Feb 28 2018	Brief amicus curiae of Wing F. Chau filed.		
	Main Document	**Certificate of Word Count**	**Proof of Service**
Feb 28 2018	Brief amicus curiae of Equity Dealers of America filed.		
	Main Document	**Certificate of Word Count**	**Proof of Service**
Feb 28 2018	Brief amicus curiae of Scholars of Corpus Linguistics filed.		
	Main Document	**Certificate of Word Count**	**Proof of Service**
Feb 28 2018	Brief amicus curiae of New Civil Liberties Alliance filed.		
	Main Document	**Certificate of Word Count**	**Proof of Service**
Mar 07 2018	CIRCULATED		
Mar 26 2018	Brief amicus curiae of Court-appointed amicus curiae in suport of the judgment below filed. (Distributed)		
	Main Document	**Certificate of Word Count**	**Proof of Service**

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RECORD AND BRIEFS

17-130

No.

Supreme Court, U.S.
FILED
JUL 21 2017
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA
AND RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

PETITION FOR A WRIT OF CERTIORARI

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Law Library

QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

All parties to the proceeding are named in the caption.

Pursuant to this Court's Rule 29.6, undersigned counsel state that petitioner Raymond J. Lucia Companies, Inc. has no parent corporation, and no publicly held company holds 10 percent or more of its stock.

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PETITION FOR A WRIT OF CERTIORARI

Petitioners Raymond J. Lucia and Raymond J. Lucia Companies, Inc. respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit.

OPINIONS BELOW

The *per curiam* order of the en banc court of appeals, denying the petition for review by an equally divided court (Pet. App. 1a-2a), is available at 2017 WL 2727019. The panel's opinion (Pet. App. 3a-36a) is reported at 832 F.3d 277. The opinion and order of the Commission (Pet. App. 37a-109a) are available at Exchange Act Release No. 73,857, 2015 WL 5172953; an interim remand order (Pet. App. 238a-243a) is unreported. The relevant initial decision of the administrative law judge (Pet. App. 115a-237a) is available at Initial Decision Release No. 495, 2013 WL 3379719.

JURISDICTION

The judgment of the court of appeals was entered on June 26, 2017. Pet. App. 1a. This Court has jurisdiction under 28 U.S.C. § 1254(1).

CONSTITUTIONAL, STATUTORY, AND REGULATORY PROVISIONS INVOLVED

The Appointments Clause as well as pertinent statutory and regulatory provisions are reproduced in the Appendix at 247a-294a.

STATEMENT

Administrative law judges of the Securities and Exchange Commission preside over trial-like adversarial hearings, during which they take testimony, rule on the admissibility of evidence, and enforce compliance with their orders. This Court has ruled that non-Article III adjudicators who exercise such discretionary powers are Officers of the United States who must be appointed pursuant to the Appointments Clause. *Freytag* v. *Comm'r*, 501 U.S. 868, 881-82 (1991). In this case, however, a three-judge panel of the D.C. Circuit ruled that SEC ALJs are mere employees who are not subject to the Appointments Clause. Pet. App. 21a. The Tenth Circuit expressly disagreed with that decision, ruling that SEC ALJs are Officers of the United States within the meaning of the Appointments Clause. *Bandimere* v. *SEC*, 844 F.3d 1168, 1170 (10th Cir. 2016). The D.C. Circuit subsequently granted en banc rehearing, but reached a 5-5 deadlock—leaving the panel decision intact and the circuit split intractable.

1. Long before the advent of the modern administrative state, the Framers understood that curbing abuses of executive power requires carefully cabining the prerogative to *appoint* those who wield it. *Edmond* v. *United States*, 520 U.S. 651, 659-60 (1997). In prescribing the exclusive means of appointing any "Office[r] of the United States," U.S. Const., art. II, § 2, cl. 2, the Appointments Clause "preserves ... the Constitution's structural integrity" by ensuring that officials invested with significant federal authority remain "accountable to political force and the will of the people." *Freytag*, 501 U.S. at 878, 884; *see also Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam).

Congress has charged the SEC with executing and enforcing the federal securities laws, 15 U.S.C. § 78d(a), including the Investment Advisers Act of 1940, *id.* § 80b-9. Congress authorized the Commission to "delegate ... any of its functions" except rulemaking to "administrative law judge[s]." *Id.* § 78d-1(a). When the Commission initiates an enforcement action, it can either sue in federal court or commence an administrative proceeding. *See id.* §§ 78u, 78u-2, 78v. Where the Commission elects to commence an administrative proceeding, an ALJ with delegated authority normally presides over the hearing. *See* 17 C.F.R. § 201.110.

In establishing this statutory scheme, Congress repeatedly referred to SEC ALJs as "officers of the Commission," 15 U.S.C. §§ 77u, 78v, 80a-40, 80b-12; set forth their duties and salary by law, *see* 5 U.S.C. §§ 556-557 (duties), 5372(b) (salary); and prescribed that the "*agency* shall appoint [its] administrative law judges," 5 U.S.C. § 3105 (emphasis added)—a manner of appointment that, if followed, would comport with the Appointments Clause.

The Commission, in turn, has deemed its ALJs "hearing officer[s]" and delegated to those "officer[s] ... the authority to do all things necessary and appropriate to discharge" their duties. 17 C.F.R. § 201.111. That authority is extensive and includes the powers to oversee hearings and discovery, rule on motions (including summary disposition), enter default judgments, and impose or modify sanctions. *See generally ibid.* (non-exhaustive list of ALJs' powers); *see also id.* §§ 201.155 (default), .180 (sanctions), .230 (document production), .232-.234 (subpoenas and depositions), .250 (summary disposition), .320-.326 (evidence). SEC ALJs also rule on the admissibility of evidence,

take testimony, and make credibility findings, to which the Commission defers absent overwhelming evidence to the contrary. Pet. App. 19a. The Commission acknowledged in this case that ALJ fact-finding plays a "vital role" in the agency's decision-making process. *Id.* 241a.

At the conclusion of an administrative hearing, SEC ALJs enter an "initial decision," 17 C.F.R. § 201.360(a)(1), that can and almost always does "become final," *id.* § 201.360(d)(2). Although the Commission "retain[s] a discretionary right to review" any "action" by an ALJ, whether *sua sponte* or upon a petition for review, 15 U.S.C. § 78d-1(b), "[i]f the right to exercise such review is declined" or not timely sought, the ALJ's action is "deemed the action of the Commission," *id.* § 78d-1(c). About 90 percent of ALJ decisions are *not* reviewed by the Commission, *see Bandimere*, 844 F.3d at 1180 n.25; in such cases, the Commission "will issue an order that the decision has become final," 17 C.F.R. § 201.360(d)(2).

It is undisputed that, if SEC ALJs are constitutional Officers, then the current procedure for their selection does not comply with the Appointments Clause. Pet. App. 9a-10a. SEC ALJs are not appointed by the Commission as a whole, but rather selected by SEC staff from a pool of candidates identified by the Office of Personnel Management. *Id.* 295a-297a (providing details of how SEC ALJs are selected).

2. Petitioner Raymond J. Lucia, formerly the sole owner of petitioner Raymond J. Lucia Companies, Inc., is an investment professional who—until this proceeding—had an unblemished record spanning nearly forty years. *See* Pet. App. 34a; 119a-120a; 233a. In free seminars for potential clients (at which

no securities were offered or sold), he promoted a retirement strategy colorfully named "Buckets of Money," which advocated a diversified portfolio from which, in retirement, investors would liquidate lower-risk investments first to give riskier investments time to grow. *Id.* 23a; 127a-129a.

Mr. Lucia used a slideshow that compared fictional investors following his strategy with investors following other strategies in hypothetical scenarios. Pet. App. 23a; 130a-132a. Two examples, which the slides described as "backtests," were based partly on historical data, such as stock returns, and partly on assumptions for other variables, such as inflation and real-estate rates of return. Both Mr. Lucia (orally) and the slides (in writing) repeatedly disclosed this use of assumptions, and the slides included dozens of disclaimers that the examples were "hypothetical." *Id.* 24a-29a; 43a n.10; 45a n.14; 76a-77a. Before Mr. Lucia publicly distributed the slideshow, supervising broker-dealers repeatedly approved the slides, and Commission staff had reviewed a similar version—and none had raised any concern that the slides were misleading. *See id.* 84a.

3. In 2012, the Commission charged petitioners with violating the anti-fraud provisions of the Investment Advisers Act of 1940 and SEC rules. Pet. App. 7a-8a. After the Commission elected to proceed administratively rather than in federal court, ALJ Cameron Elliot presided over a trial-like hearing at which witnesses testified and were cross-examined, documents were introduced into evidence, and objections were made and ruled upon. After Judge Elliot issued an initial decision, the Commission remanded for further factual findings, *id.* 239a, because they

were "a matter of considerable importance" to the Commission, *id.* 241a.

On remand, Judge Elliot found that Mr. Lucia's presentations were misleading because they used the word "backtest"—a term with no statutory or regulatory definition—to describe hypotheticals that were not based solely on historical data, but included certain disclosed assumptions. Pet. App. 115a-116a; 196a-197a. Despite finding that the SEC had not proved any investor losses, Judge Elliot barred Mr. Lucia from working as an investment advisor for the rest of his life, revoked his company's registration, and assessed civil penalties. *Id.* 225a-233a. Because of these sanctions, Mr. Lucia is unemployable in his lifelong profession and on the verge of bankruptcy.

4. Petitioners timely sought Commission review, challenging the initial decision on the merits and arguing that Judge Elliot held office in violation of the Appointments Clause. Pet. App. 38a-40a. The Commission granted discretionary review and—by a 3-2 vote—affirmed in relevant part. *Ibid.*; *id.* 110a.

On the merits, the Commission majority sustained Judge Elliot's finding that the presentations were misleading because a "backtest" must use "historical data" whereas petitioners' hypotheticals relied in part on assumptions. Pet. App. 66a-69a. Relying on *Landry* v. *FDIC*, 204 F.3d 1125 (D.C. Cir. 2000), the Commission majority further concluded that SEC ALJs are "not subject to the requirements of the Appointments Clause," Pet. App. 86a, because "it is 'the Commission's issuance of a finality order' that makes [an ALJ's] decision effective and final," *id.* 90a.

In the SEC's only written dissent of 2015, Commissioners Gallagher and Piwowar sharply disagreed

on the merits. *See* Pet. App. 110a-114a. The dissenters explained that the majority had "create[d] from whole cloth specific requirements for advertisements that include the word 'backtest,'" and then applied to petitioners a new rule deeming it misleading "if a backtest fails to use actual historical rates—even if the slideshow presentation specifically discloses the use of assumed rates for certain components." *Id.* 111a. The dissenters also noted that Article III courts should decide the Appointments Clause issue. *Id.* 113a.

5. A three-judge panel of the D.C. Circuit denied a timely petition for review. Pet. App. 4a. In addition to sustaining the Commission's decision on the merits, *id.* 21a-36a, the panel rejected petitioners' Appointments Clause challenge.

The panel stated that, under the D.C. Circuit's 2-1 decision in *Landry*, the constitutional "analysis begins, and ends," with "whether Commission ALJs issue final decisions of the Commission." Pet. App. 13a. Petitioners argued both that *Landry*'s approach was inconsistent with *Freytag*, which rejected the argument that adjudicators "may be deemed employees ... because they lack authority to enter a final decision," 501 U.S. at 881, and that applying *Landry* here would be inconsistent with *Edmond*'s holding that certain military appellate judges were Officers even though their decisions were subject to discretionary review. *See* Pet. App. 13a. But the panel summarily responded that "this court has rejected that argument, and *Landry* is the law of the circuit." *Ibid.*

Relying solely on *Landry*, the panel held that SEC ALJs are not Officers because their decisions are subject to discretionary Commission review and, therefore, are not independently final. Pet. App. 13a-18a.

The panel concluded that "the Commission has retained full decision-making powers" in every case because an ALJ's "initial decision becomes final when, and only when, the Commission issues [a] finality order." *Id.* 15a.

Petitioners timely filed a petition for rehearing en banc, arguing that the panel decision could not be reconciled with this Court's Appointments Clause jurisprudence. Petitioners also pointed out that, in opposing certiorari in *Landry*, the government had defended *Landry* as limited to one particular agency, *see* Br. in Opp. 7, *Landry* v. *FDIC*, No. 99-1916 (U.S. Aug. 28, 2000), 2000 WL 34013905 ("*Landry* BIO"), but reneged on that promise in this case by arguing that *Landry* resolved the Appointments Clause question for all ALJs.

While that petition was pending, the Tenth Circuit ruled that SEC ALJs *are* Officers of the United States who must be appointed pursuant to the Appointments Clause. *Bandimere*, 844 F.3d at 1179, 1188. The Tenth Circuit majority expressly disagreed with the D.C. Circuit's reasoning: "*Landry* place[s] undue weight on final decision-making authority." *Id.* at 1182. As Judge Briscoe explained, "[t]he critical difference between the [*Bandimere*] majority and *Landry* and *Lucia* is that the majority recognizes that *Freytag* does *not* make final decision-making authority the *sine qua non* of inferior Officer status." *Id.* at 1189 (concurring opinion). The government filed a petition for rehearing that was "transmitted to all the judges of the court who are in regular active service" and then, after Justice Gorsuch's confirmation, denied by a 9-2 vote. *Bandimere* v. *SEC*, 855 F.3d 1128 (10th Cir. 2017).

In light of these conflicting decisions, the D.C. Circuit granted rehearing en banc to resolve two questions: (1) "Is [Judge Elliot] an inferior officer rather than an employee for the purposes of the Appointments Clause of Article II of the Constitution?"; and (2) "Should the court overrule [*Landry*]?" Pet. App. 245a. Under the D.C. Circuit's rules, a grant of en banc rehearing vacates the panel's judgment but "ordinarily not its opinion." D.C. Cir. R. 35(d).

The ten judges comprising the en banc court heard argument on May 24, 2017. *Hear* Oral Argument, *Raymond J. Lucia Cos., Inc.* v. *SEC*, 2017 WL 2727019 (D.C. Cir. June 26, 2017) (en banc) (No. 15-1345), https://tinyurl.com/yddcpeyh (all Internet sites last visited July 17, 2017). A month later, the court issued a brief *per curiam* order and judgment stating that the petition for review was denied by an equally divided court. Pet. App. 1a-2a (citing D.C. Cir. R. 35(d)).

REASONS FOR GRANTING THE PETITION

The D.C. Circuit—which hears more petitions for review of SEC action than any other court of appeals—granted en banc rehearing to decide whether SEC ALJs are constitutional Officers, and then deadlocked 5-5 on that question, confirming that this Court's review is required. *Cf. Alice Corp. Pty., Ltd.* v. *CLS Bank Int'l*, 134 S. Ct. 2347, 2353-54 (2014) (granting review after en banc court of appeals failed to produce majority opinion resolving recurring issue). Moreover, the en banc court's inability to resolve the Appointments Clause issue leaves in place a square and acknowledged conflict between the panel decision in this case, which held that SEC ALJs are mere employees, and the Tenth Circuit's contrary holding that SEC ALJs are Officers of the United States. *Compare*

Pet. App. 21a *with Bandimere* v. *SEC*, 844 F.3d 1168, 1188 (10th Cir. 2016). Only this Court can resolve this conflict. This case cleanly presents the important and recurring question whether SEC ALJs are Officers who must be appointed pursuant to the Appointments Clause.

I. SEC ALJs Are Officers Of The United States

This Court's precedents make clear that the Appointments Clause's purposefully broad category of "Officers" includes SEC ALJs because they exercise significant discretion in conducting trials, making evidentiary and other rulings that shape the administrative record, and issuing initial decisions that become final in 90 percent of cases.

A.1. This Court has consistently applied a simple, expansive definition of "Officer": Every official whose position is "established by Law" and who exercises "significant authority pursuant to the laws of the United States is an 'Officer of the United States.'" *Buckley* v. *Valeo*, 424 U.S. 1, 126, 132 (1976) (per curiam) (quoting U.S. Const. art. II, § 2, cl. 2). "Unless their selection is elsewhere provided for" in the Constitution—as with the President—"*all* officers of the United States" who meet these criteria "are to be appointed in accordance with the Clause." *Id.* at 132.

Buckley's broad definition of "Officer" makes perfect sense of the Clause's text. *See, e.g.*, 2 Samuel Johnson, *A Dictionary of the English Language*, s.v. "officer" (6th ed. 1785) ("A man employed by the publick"); 2 Noah Webster, *An American Dictionary of the English Language*, s.v. "officer" (1828) (similar). And it is pivotal to the "structural safeguar[d]" the text provides. *Edmond* v. *United States*, 520 U.S. 651, 659

(1997). The Framers viewed "'the power of appointment to offices'" as "'the most insidious and powerful weapon of eighteenth century despotism.'" *Freytag* v. *Comm'r*, 501 U.S. 868, 883 (1991) (citation omitted). They "understood ... that by limiting the appointment power" to those who were readily identifiable, "they could ensure that those who wielded it were accountable to political force and the will of the people." *Id.* at 884. The Clause's restrictions thus "preserv[e] ... the Constitution's structural integrity by preventing the diffusion of the appointment power." *Id.* at 878.

The Court's modern definition of "Officer" reflects two centuries of decisions holding a wide range of officials to be subject to the Clause—including:

- district-court clerks, *Ex parte Hennen*, 38 U.S. (13 Pet.) 230, 258 (1839);
- a clerk to an assistant treasurer in Boston, *United States* v. *Hartwell*, 73 U.S. (6 Wall.) 385, 393-94 (1868);
- engineers and assistant surgeons, *United States* v. *Perkins*, 116 U.S. 483, 484 (1886); *United States* v. *Moore*, 95 U.S. 760, 762 (1878);
- "thousands of clerks in the Departments of the Treasury, Interior and the othe[r]" departments, *United States* v. *Germaine*, 99 U.S. 508, 511 (1879), responsible for "the records, books, and papers appertaining to the office," *Hennen*, 38 U.S. (13 Pet.) at 259;
- judges of election and federal marshals, *Ex parte Siebold*, 100 U.S. 371, 397-99 (1880);
- "commissioners of the circuit courts" who "t[ook] ... bail for the appearance of persons

charged with crime," *United States* v. *Allred*, 155 U.S. 591, 594 (1895);

- extradition commissioners, *Rice* v. *Ames*, 180 U.S. 371, 378 (1901);
- district-court commissioners, *Go-Bart Importing Co.* v. *United States*, 282 U.S. 344, 352-54 (1931); and
- U.S. attorneys, *Myers* v. *United States*, 272 U.S. 52, 159 (1926).

Only individuals with "no general functions, nor any employment which has any duration as to time," whose posts lack "tenure, duration, continuing emolument, or continuous duties," and who "ac[t] only occasionally and temporarily" have been held by this Court to fall outside the Clause. *Auffmordt* v. *Hedden*, 137 U.S. 310, 327 (1890); *see also Buckley*, 424 U.S. at 126 n.162 (employees are "lesser functionaries subordinate to" Officers).

2. This Court has *never* held that a federal adjudicator is a mere employee, while holding that many quasi-judicial officials—including clerks, commissioners, and non-Article III judges—*are* Officers. *See generally* Jennifer L. Mascott, *Who Are 'Officers of the United States'?*, 70 Stan. L. Rev. (forthcoming 2017) (draft at https://tinyurl.com/zewj8z2); Kent Barnett, *Resolving the ALJ Quandary*, 66 Vand. L. Rev. 797, 799-803, 810-14 (2013). For example, court commissioners (the predecessors of today's magistrate judges) are constitutional Officers. *Go-Bart*, 282 U.S. at 352-54; *Allred*, 155 U.S. at 594. There is no difference of constitutional magnitude between magistrate judges and administrative law judges.

The critical decision is *Freytag*, in which this Court held that special trial judges of the U.S. Tax

Court are Officers. 501 U.S. at 880-82. Although STJs could make final decisions in some cases, in other cases (including *Freytag* itself) they lacked final decision-making power and could issue only proposed opinions, which the Tax Court was free to accept or reject. *Ibid.* *Freytag* unanimously held that, even in such cases, STJs acted as Officers because they "exercised significant discretion" in performing "important functions"—specifically, "tak[ing] testimony," "conduct[ing] trials," "rul[ing] on the admissibility of evidence," and "enforc[ing] compliance with discovery orders." *Id.* at 881-82; *accord id.* at 901 (Scalia, J., concurring in part and concurring in the judgment).

This Court has held that military judges, too, are Officers based on their significant adjudicatory duties. In *Weiss* v. *United States*, 510 U.S. 163 (1994), the Court explained that military judges are Officers "because of the authority and responsibilities [they] possess," which include ruling on procedural and legal issues and adjudicating offenses under the Uniform Code of Military Justice. *Id.* at 167-69; *see also Ryder* v. *United States*, 515 U.S. 177, 180-88 (1995). This Court's decision in *Edmond* likewise recognized that intermediate appellate military judges are Officers, in part because they "independently 'weigh the evidence, judge the credibility of witnesses, and determine controverted questions of fact.'" 520 U.S. at 662 (quoting 10 U.S.C. § 866(c)). That the judges "ha[d] no power to render a final decision" on their own was relevant only to whether they were "inferior officers" or "principal officers." *Id.* at 665-66.

B. Under these principles and precedents, SEC ALJs are "Officers" subject to the Appointments Clause. It is not disputed that SEC ALJs hold offices established by law, or that they exercise authority—

including ruling on the admissibility of evidence, taking testimony, and conducting trials—previously deemed sufficiently "significant" to confer Officer status. *Freytag*, 501 U.S. at 881-82. This Court need go no further to conclude that SEC ALJs are Officers.

Like the special trial judges in *Freytag*, SEC ALJs' "duties, salary, and means of appointment" all "are specified by statute," 501 U.S. at 881; *see* 5 U.S.C. §§ 556-557, 3105, 5372. Congress in fact *referred* to SEC ALJs as "officers" in the securities laws. 15 U.S.C. § 77u ("[a]ll hearings ... may be held before the Commission or an *officer* or *officers* of the Commission designated by it" (emphases added)); *see id.* §§ 78v, 80a-40, 80b-12 (same). Federal law accordingly provides that the "*agency*"—here, the Commission—"shall appoint ... administrative law judges." 5 U.S.C. § 3105 (emphasis added); *see Free Enter. Fund* v. *PCAOB*, 561 U.S. 477, 512-13 (2010) (SEC Commissioners acting as a body constitute a "Head of Department" under the Clause). The SEC has never explained why the Commission itself does not—or could not—appoint its ALJs.

SEC ALJs also "'exercis[e] significant authority pursuant to the laws of the United States,'" *Freytag*, 501 U.S. at 881 (quoting *Buckley*, 424 U.S. at 126), entrusted to them by the federal securities laws and the Commission. That authority includes the power to "conduc[t] hearings in proceedings instituted by the Commission," and "to do all things necessary and appropriate to discharge" that function. 17 C.F.R. § 200.14. Specific duties include:

- amending charging documents, *id.* § 201.200(d)(2);
- entering orders of default, *id.* § 201.155;

- consolidating proceedings, *id.* § 201.201(a);
- "[a]dminister[ing] oaths and affirmations," *id.* §§ 200.14(a)(1), 201.111(a);
- "[i]ssu[ing] subpoenas," *id.* §§ 200.14(a)(2), 201.111(b);
- ordering depositions and acting as the "deposition officer," *id.* §§ 201.233-.234;
- ordering production of evidence and regulating document production, *id.* §§ 201.111(b), .230, .232;
- issuing protective orders, *id.* § 201.322;
- "[r]ul[ing] upon motions," including for summary disposition, *id.* §§ 200.14(a)(7), 201.111(h), .250;
- rejecting filings for procedural noncompliance, *id.* § 201.180(b);
- granting extensions of time and stays, *id.* § 201.161;
- "[h]old[ing] pre-hearing conferences" and "requir[ing]" attendance at such conferences, *id.* §§ 200.14(a)(6), 201.111(e), .221(b);
- ordering prehearing submissions, *id.* § 201.222(a);
- "[r]egulat[ing] the course of [the] hearing," *id.* §§ 200.14(a)(5), 201.111(d);
- receiving "relevant evidence" and ruling upon admissibility, *id.* § 201.111(c);
- "[r]ul[ing] on offers of proof," *id.* §§ 200.14(a)(3), 201.111(c);
- "[e]xamin[ing] witnesses," *id.* § 200.14(a)(4);

- regulating the scope of cross-examination, *id.* § 201.326;
- regulating "the conduct of the parties and their counsel," *id.* § 201.111(d); and
- imposing sanctions for "contemptuous conduct," *id.* § 201.180(a).

These are *adjudicatory* functions that, under *Freytag*, reflect Officer status. *Bandimere*, 844 F.3d at 1187 ("STJs and ALJs closely resemble one another where it counts"). To be sure, ALJs cannot impose fines or imprisonment for contempt (although they can impose other sanctions against contumacious litigants or attorneys), but that is true of most administrative agency officials. *See ICC* v. *Brimson*, 154 U.S. 447, 488-89 (1894). Indeed, the statute that grants the Tax Court contempt power, 26 U.S.C. § 7456(c), does not grant STJs the same power. And this Court has never hinted that contempt power is even relevant to Officer status.

In addition to performing the same functions found significant in *Freytag* (and then some), the SEC ALJ, following a hearing, "prepare[s] an initial decision containing the conclusions as to the factual and legal issues presented." 17 C.F.R. §§ 200.14(a)(8), 201.111(i), .141(b), .360(a). Although parties may petition for review of the ALJ's initial decision by the Commission, or the Commission may review the decision *sua sponte*, *see id.* § 201.410(a), review of an ALJ decision is the exception: In approximately 90 percent of cases, no such further review is conducted. *See Bandimere*, 844 F.3d at 1180 n.25; SEC, ALJ Initial Decisions, https://www.sec.gov/alj/aljdec.shtml. Review often is not sought, and even when requested it is not always granted. *See* 17 C.F.R. § 201.411(b)(2)

(the Commission can "decline to review any [ALJ] decision," except in limited circumstances not pertinent here); *see also, e.g.*, *In re Bellows*, Exchange Act Release No. 40,411, 1998 WL 611766 (Sept. 8, 1998) (declining such review). SEC ALJs also have power to issue default orders that are immediately judicially "enforceable" without *any* SEC review. *In re Alchemy Ventures, Inc.*, Exchange Act Release No. 70,708, 2013 WL 6173809, at *4 (Oct. 17, 2013).

If no timely petition for review is filed or if the Commission declines review, the ALJ's initial decision by statute "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. § 78d-1(c); *accord* 5 U.S.C. § 557(b) (ALJs' "initial decisions" automatically become final "without further proceedings" absent further review). In such cases, the Commission's regulations provide that it "will issue an order that the [ALJ's] decision has become final." 17 C.F.R. §§ 201.360(a)(1), .360(d)(2). The finality order is non-discretionary and issues as a matter of course after 42 days when no petition for review has been filed. *See id.* §§ 201.360(d)(2), .410(b), .411(c).

On the relatively rare occasions the Commission *does* review an ALJ's initial decision, the Commission does not review the decision anew, but defers to the ALJ's credibility determinations and factual findings. *See In re Clawson*, Exchange Act Release No. 48,143, 2003 WL 21539920, at *2 (July 9, 2003) ("We accept [an SEC ALJ's] credibility finding, absent *overwhelming evidence* to the contrary" (emphasis added)); *In re Bridge*, Securities Act Release No. 9,068, 2009 WL 3100582, at *18 n.75 (Sept. 29, 2009) (similar). As the Commission emphasized in this case, SEC ALJs play a "vital role" in the adjudicative process, as they are

"'in the best position to make findings of fact ... and resolve any conflicts in the evidence.'" Pet. App. 241a (citation omitted). Judge Elliot is the only adjudicator in this case who saw and heard the witnesses testify, who reviewed all the evidence, and who shaped the record through evidentiary and other rulings. *See, e.g., id.* 193a (finding an Enforcement Division witness credible after noting that evidence concerning a false claim brought by that witness had previously been excluded).

The authority of SEC ALJs mirrors that of the STJs in *Freytag* (as well as the military judges in *Weiss* and *Edmond*). Indeed, the SEC itself represents to the public that its ALJs perform comparable functions to *federal district judges*. SEC, Office of Administrative Law Judges, https://www.sec.gov/alj (last modified Jan. 26, 2017) (ALJs "conduct public hearings ... in a manner similar to non-jury trials in the federal district courts"); *see also* SEC, SEC Announces Arrival of New Administrative Law Judge Cameron Elliot, http://www.sec.gov/news/press/2011/2011-96.htm (Apr. 25, 2011). This Court has similarly observed that "the role of the modern ... administrative law judge ... is 'functionally comparable' to that of a judge." *Butz* v. *Economou*, 438 U.S. 478, 513 (1978). A number of Justices, in fact, have previously indicated that ALJs in general are Officers. *See Free Enter. Fund*, 561 U.S. at 542 (Breyer, J., joined by Stevens, Ginsburg, and Sotomayor, JJ., dissenting); *Freytag*, 501 U.S. at 910 (Scalia, J., joined by O'Connor, Kennedy, and Souter, JJ., concurring in part and concurring in the judgment).

Until recently, the Executive Branch agreed that officials with the authority of ALJs are Officers. The Office of Legal Counsel—responsible for providing

"authoritative legal advice" for the Executive Branch (DOJ, Office of Legal Counsel, http://www.justice.gov/olc)—opined that an "'Office[r] of the United States'" is one who "possesses delegated sovereign authority to act in the first instance, *whether or not that act may be subject to direction or review by superior officers*." *Officers of the U.S. Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73, 95 (2007) (emphasis added). That opinion has never been withdrawn or disavowed by the President or the Attorney General, and it is flatly contrary to the D.C. Circuit's finality requirement and the SEC's litigating position in this case. It makes clear that "[n]either *Buckley* nor early authority supports [a] restriction" of Officer status to exclude those who "'act only at the direction of'" other Officers. *Id.* at 93 (citation omitted).

Under this Court's established (and unbroken) line of Appointments Clause jurisprudence, SEC ALJs are Officers of the United States within the meaning of the Clause.

II. THERE IS A DIRECT AND ACKNOWLEDGED CIRCUIT SPLIT ON THE QUESTION PRESENTED

Two courts of appeals have now applied this body of precedent to reach conflicting decisions on whether SEC ALJs are Officers of the United States who must be appointed pursuant to the Appointments Clause. The D.C. Circuit panel answered that question in the negative, while the Tenth Circuit answered it in the affirmative. The question presented is binary; one of these two decisions *must* be wrong. Indeed, at each step in the analysis the Tenth Circuit squarely "disagree[d]" with the panel decision left in place by the en banc court's order. *Bandimere*, 844 F.3d at 1182. Moreover, the judgment in this case denying the peti-

tion for review is irreconcilable with the Tenth Circuit's judgment granting a petition for review based on the identical constitutional challenge. *Compare* Pet. App. 2a *with Bandimere*, 844 F.3d at 1188. Certiorari is necessary to resolve this dispute between the circuits on an important and recurring constitutional issue.

A. The D.C. Circuit Wrongly Concluded That SEC ALJs Are Mere Employees

The panel decision never addressed the many important, and discretionary, duties exercised by SEC ALJs discussed above. Instead, it held that under *Landry* its "analysis begins, and ends," with whether SEC ALJs can issue unreviewable final decisions of the Commission, and concluded that they cannot. Pet. App. 13a; *see also Bandimere*, 844 F.3d at 1182 ("The D.C. Circuit followed *Landry*" and "considered dispositive" SEC ALJs' supposed "inability to render final decisions"). Confining the Appointments Clause's reach to those who have the power of final decision, however, contravenes this Court's teaching in *Freytag*. At minimum, confining the Clause's reach to those who can issue *unreviewable* final decisions cannot be reconciled with this Court's teaching in *Edmond*.

1. The panel decision uncritically adopted its finality requirement from the D.C. Circuit's divided decision in *Landry*, Pet. App. 13a, which held that inferior Officers must have the "power of final decision," 204 F.3d at 1134. *This* Court's precedents make clear, though, that authority to issue final decisions is a criterion that distinguishes inferior Officers from principal Officers, not a *sine qua non* for the Clause to apply at all.

Freytag expressly rejected the argument that inability to make final decisions takes officials outside the Appointments Clause. 501 U.S. at 880-82. In many cases, including *Freytag* itself, STJs "lack[ed] authority to enter a final decision," and merely "assist[ed]" other officials "in taking the evidence and preparing the proposed findings and opinion." *Ibid.* That did not matter, *Freytag* held, and deeming those judges mere employees on that basis would "ignor[e] the significance of the duties and discretion that [the] judges possess"—namely, the fact that they "perform[ed] more than ministerial tasks," including "tak[ing] testimony," "conduct[ing] trials," and "rul[ing] on the admissibility of evidence." *Ibid.*

To be sure, the *Freytag* Court went on to hold in the alternative that "*[e]ven if* the duties of special trial judges ... were not as significant as we ... have found them to be, our conclusion would be unchanged" because STJs could issue final decisions in *other* cases. 501 U.S. at 882 (emphasis added). But as Judge Randolph cogently explained, that "conclusion" was "[t]he conclusion" the Court "had reached in the preceding paragraphs"—"namely, that although special trial judges may not render final decisions, they are nevertheless inferior officers of the United States." *Landry*, 204 F.3d at 1142 (concurring opinion); *see Freytag*, 501 U.S. at 881. The power of final decision in *Freytag* is thus "clearly designated ... as an alternative holding." *Landry*, 204 F.3d at 1142 (Randolph, J., concurring). While authority to make final decisions may be *sufficient* to trigger the Appointments Clause, the Appointments Clause hardly makes such authority *necessary*—and under this Court's precedent it is not.

The panel in this case summarily rejected petitioners' argument that *Landry*'s contrary reasoning

was "inconsistent with *Freytag*," stating that "*Landry* is the law of the circuit." Pet. App. 13a. But *Landry* was wrongly decided, as Judge Randolph pointed out at the time. *See* 204 F.3d at 1140-43 (concurring opinion). Time and again, this Court has held that adjudicators who lacked final decision-making authority nevertheless were constitutional Officers. *See, e.g.*, *Go-Bart*, 282 U.S. at 352, 354 ("All the [Officer's] acts ... were preparatory and preliminary to a consideration of the charge by a grand jury and ... the final disposition of the case in the district court"); *Allred*, 155 U.S. at 595 (commissioners are "subject to the orders and directions of the court appointing them"); *accord Weiss*, 510 U.S. at 168 ("No sentence imposed [by the Officer] becomes final until it is approved by the officer who convened the court-martial"). Since these officials all are Officers notwithstanding their lack of final decision-making authority, such authority *cannot* be the lynchpin of Officer status as the court below made it.

2. The panel decision not only erroneously confined the Appointments Clause to officials with final decision-making authority, but also implausibly extended that requirement to exempt officials who *can and do* issue final decisions, so long as those decisions are subject to "'discretionary ... review.'" Pet. App. 14a-18a. That holding cannot be reconciled with this Court's decision in *Edmond*.

Edmond held that judges on the Coast Guard Court of Criminal Appeals were inferior Officers because their decisions were always subject to further review by principal Officers—namely, the Court of Appeals for the Armed Forces—whether by *sua sponte* order of the Judge Advocate General or where the CAAF exercised its discretion to grant review.

520 U.S. at 664-65; *see* 10 U.S.C. § 867(a). The lack of "power to render a final decision ... unless permitted to do so by other Executive officers," *Edmond* held, is the defining *feature* of "'inferior officers,'" distinguishing them from the "'principal officer[s]'" that supervise them. 520 U.S. at 663, 665; *see also Dep't of Transp.* v. *Ass'n of Am. R.Rs.*, 135 S. Ct. 1225, 1239 (2015) (Alito, J., concurring) ("Inferior officers can do many things, but nothing final should appear in the Federal Register unless a Presidential appointee has at least signed off on it").

As the United States has represented to this Court on at least two occasions, "*Edmond* makes clear [that] ... inability to render a *final* decision" is "indicative of inferior ... officer status." U.S. Br. 32 n.10, *Free Enter. Fund* v. *PCAOB*, No. 08-861 (U.S. Oct. 13, 2009), 2009 WL 3290435 (emphasis omitted); *see also Landry* BIO 12 n.4 ("In concluding that judges on the Coast Guard Court of Criminal Appeals are 'inferior' rather than 'principal' officers, the Court in *Edmond* observed that those judges 'have no power to render a final decision on behalf of the United States *unless permitted to do so by other Executive officers*'").

The panel nevertheless held that SEC ALJs are employees, not Officers, precisely because their decisions are subject to discretionary review. That holding cannot be squared with *Edmond* or, indeed, any other decision where this Court held that an official who cannot render an unreviewable final decision of the Executive Branch is nevertheless an Officer:

Case	Adjudicator	Officer?	Unreviewable Final Decisions?
Go-Bart, 282 U.S. 344	U.S. Commissioners	**Yes.** 282 U.S. at 352.	**No.** 282 U.S. at 354.
Allred, 155 U.S. 591	U.S. Circuit Commissioners	**Yes.** 155 U.S. at 594-95.	**No.** 155 U.S. at 595.
Weiss, 510 U.S. 163	Military judges	**Yes.** 510 U.S. at 169.	**No.** 510 U.S. at 168.
Ryder, 515 U.S. 177	Judges of the Coast Guard Court of Military Review	**Yes.** 515 U.S. at 180-88.	**No.** *Edmond*, 520 U.S. at 653, 665.
Edmond, 520 U.S. 651	Judges of the Coast Guard Court of Criminal Appeals	**Yes.** 520 U.S. at 662-66.	**No.** 520 U.S. at 665.
Free Enter. Fund, 561 U.S. 477	Public Company Accounting Oversight Board	**Yes.** 561 U.S. at 486.	**No.** 537 F.3d at 673.

Even federal *magistrates*—who wield wide authority and plainly are Officers under *Buckley*—would not be Officers under the D.C. Circuit's test because they cannot (absent consent) render final decisions on the merits. *See* 28 U.S.C. § 636(b)(1)(A).

In short, the D.C. Circuit's finality rule conflates a prerequisite for principal-Officer status with a gateway requirement for the Appointments Clause to apply at all. As *Edmond* explained, the very term "'inferior officer' connotes a relationship with some higher ranking officer"; their "work is directed and supervised" by such "'principal officer[s].'" 520 U.S. at 662-63; *see also NLRB* v. *SW Gen., Inc.*, 137 S. Ct. 929, 947 (2017) (Thomas, J., concurring) ("a principal officer is one who has no superior other than the President"). The Appointments Clause by its terms covers *both* types of Officers, simply allowing (at Congress's option) a different appointment method for the latter. U.S. Const. art. II, § 2, cl. 2. The D.C. Circuit's finality rule, however, effectively confines the Clause to *only* principal Officers, *i.e.*, those with power to make unreviewable final decisions. If the decision below were allowed to stand, it would erase the category of "inferior Officers" from the text of our Constitution.

3. The panel decision noted that Congress "provid[ed] Civil Service protections to ALJs in response to concerns their actions were influenced by a desire to curry favor with agency heads." Pet. App. 21a (citing *Ramspeck* v. *Fed. Trial Exam'rs Conference*, 345 U.S. 128, 132 & n.3, 142 (1953)). The effectiveness of this structure might be questioned given that in roughly 50 decisions before this one, Judge Elliot had not once ruled against the Commission. *See* Sarah N. Lynch, *SEC Judge Who Took on the "Big Four" Known for Bold Moves*, Reuters (Feb. 3, 2014), https://tinyurl.com/hlu76fl. To be sure, the Commission exercised its power of discretionary review and (by a 3-2 margin) affirmed his decision; but that establishes only that Judge Elliot is an inferior rather than a principal Officer. *See Edmond*, 520 U.S. at 665.

In any event, individuals with civil service protections may be Officers. *See, e.g., Cw. of Pennsylvania* v. *U.S. Dep't of HHS*, 80 F.3d 796, 801-04, 806 (3d Cir. 1996). Indeed, contemporaneously with *Ramspeck* the Attorney General opined that hearing examiners—the predecessors to ALJs—were "inferior officers" even though their pay, promotion, and termination were controlled by the Civil Service Commission. *Administrative Procedure Act, Promotion of Hearing Examiners*, 41 Op. Att'y Gen. 74, 79-80 (1951).

As *Ramspeck* explained, "Congress intended to make hearing examiners 'a special class of semi-independent subordinate hearing *officers*.'" 345 U.S. at 132 (emphasis added) (citation omitted). When Congress originally enacted the Administrative Procedure Act of 1946, it thus referred to hearing examiners as "officers" *nine* times. *See* Administrative Procedure Act, Pub. L. No. 79-404, 60 Stat. 237 (1946). And in enacting the securities laws, Congress referred to ALJs as "officers," prescribing that "[a]ll hearings ... may be held before the Commission or an *officer* or *officers* of the Commission." 15 U.S.C. § 77u (emphases added); *see also id.* §§ 78v, 80a-40, 80b-12 (same).

The panel here said that "there is no indication Congress intended these officers to be synonymous with 'Officers of the United States' under the Appointments Clause." Pet. App. 21a. But this Court has squarely rejected this very argument. *Germaine*, 99 U.S. at 510 (if Congress's use of "officers" had meant "others than officers as defined by the Constitution, words to that effect would be used, as servant, agent, person in the service or employment of the government"). The panel's decision runs headlong into this precedent and the rest of this Court's Appointments Clause jurisprudence.

B. The Tenth Circuit Correctly Held That SEC ALJs Are Officers

The Tenth Circuit has held—on materially indistinguishable facts—that "SEC ALJs are inferior officers who must be appointed in conformity with the Appointments Clause." *Bandimere*, 844 F.3d at 1181. The result in *Bandimere* shows that there is a conflict among the circuits that requires this Court's intervention; its reasoning points up the errors made by the panel in this case.

1. *Bandimere*, like this case, concerned an SEC administrative action resulting in a lifetime industry bar and civil penalties. 844 F.3d at 1171. In affirming the ALJ's initial decision on discretionary review, *ibid.*, the Commission again relied on the D.C. Circuit's decision in *Landry* and concluded that SEC ALJs are not "Officers" within the meaning of the Appointments Clause. *In re Bandimere*, Securities Act Release No. 9,972, 2015 WL 6575665, at *19-21 (Oct. 29, 2015).

The Tenth Circuit granted the petition for review and vacated the Commission's decision, holding that SEC ALJs are inferior Officers because they "carry out 'important functions,'" *Bandimere*, 844 F.3d at 1188 (quoting *Freytag*, 501 at 882), and "'exercis[e] significant authority pursuant to the laws of the United States,'" *ibid.* (quoting *Buckley*, 424 U.S. at 126). *Bandimere* recognized that, although this Court "has not stated a specific test for inferior officer status ... 'the term's sweep is unusually broad.'" *Id.* at 1174 (quoting *Free Enter. Fund*, 561 U.S. at 539 (Breyer, J., dissenting)). Drawing from its review of the 150-year history of this Court's cases "contain[ing] examples of inferior officers," the Tenth Circuit concluded that "*Freytag* controls the result." *Id.* at 1173-74. The

court gleaned "three characteristics" of inferior Officers from *Freytag*: (1) their position is "'established by Law'"; (2) their "'duties, salary, and means of appointment ... are specified by statute'"; and (3) they "'exercise significant discretion' in 'carrying out ... important functions.'" *Id.* at 1179 (alterations in original) (quoting *Freytag*, 501 U.S. at 881-82).

As *Bandimere* explained, "[t]hose three characteristics exist" with respect to SEC ALJs. 844 F.3d at 1179. *First*, both the position and the delegated powers of SEC ALJs are established by law. *Ibid.* (citing 5 U.S.C. § 556(b)(3); 17 C.F.R. § 200.14). *Second*, various statutes set forth the duties, salary, and means of appointment of SEC ALJs. *Ibid.* (citing 5 U.S.C. §§ 556-557 (duties); *id.* § 5372(b) (salary); *id.* §§ 1302, 3105 (means of appointment)). *Third*, SEC ALJs "exercise significant discretion in performing 'important functions' commensurate with the STJs' functions described in *Freytag*." *Ibid.* "[B]oth perform similar adjudicative functions," the majority reasoned: "They take testimony, conduct trials, rule on admissibility of evidence, and have the power to enforce compliance with discovery orders." *Id.* at 1181 & n.30 (quoting *Freytag*, 501 U.S. at 881-82).

Bandimere also "spell[ed] out even more of [the] discretionary functions" exercised by SEC ALJs. 844 F.3d at 1181 n.30. For example, SEC ALJs can "shape the administrative record by taking testimony, regulating document production and depositions, ruling on the admissibility of evidence, receiving evidence, ruling on dispositive and procedural motions, issuing subpoenas, and presiding over trial-like hearings." *Id.* at 1179-80 (footnotes omitted). SEC ALJs also "make credibility findings to which the SEC affords 'considerable weight' during agency review,"

"enter default judgments and otherwise steer the outcome of proceedings by holding and requiring attendance at settlement conferences," and "issue initial decisions that declare respondents liable and impose sanctions." *Id.* at 1180-81 (footnotes omitted) (quoting *Bandimere*, 2015 WL 6575665, at *15 n.83). Because SEC ALJs "closely resemble the STJs described in *Freytag*," the Tenth Circuit held that SEC ALJs "are inferior officers who must be appointed as the Constitution commands." *Id.* at 1181.

Judge Briscoe concurred, "fully join[ing]" the majority, and writing separately to explain that an Appointments Clause challenge "requires a position-by-position analysis of the authority Congress by law and a particular executive agency by rule and practice has delegated to its personnel." *Bandimere*, 844 F.3d at 1189 (concurring opinion). "[S]weeping pronouncements" on the constitutional status of other ALJs, Judge Briscoe continued, would be both unnecessary and inappropriate. *Ibid.* This was a pointed response to Judge McKay's dissent, which consisted in large part of such sweeping pronouncements. *See id.* at 1194, 1199-1201 (dissenting opinion).

2. The Tenth Circuit acknowledged that it was "address[ing] the same question," yet reaching the opposite conclusion, as the panel decision in this case. *Bandimere*, 844 F.3d at 1182. The Tenth Circuit expressly rejected both *Landry*'s finality requirement for Officer status *and* the panel's extension of that requirement in this case.

a. Whereas the D.C. Circuit held that under *Landry*, the constitutional analysis "begins, and ends," with whether SEC ALJs "issue final decisions of the Commission," Pet. App. 13a, *Bandimere* expressly rejected the "final authority argument ... that

the D.C. Circuit relied on in *Landry* and *Lucia*." 844 F.3d at 1186; *see also id.* at 1182 ("We disagree ... that final decision-making power is dispositive to the question at hand"). Beginning and ending the Appointments Clause analysis with an official's final decision-making authority, the Tenth Circuit explained, would "ignor[e] the significance of the duties and discretion that [the official] possess[es]," *id.* at 1175 (quoting *Freytag*, 501 U.S. at 881), and "place undue weight" on a factor that, though perhaps "*relevant* in determining whether a public servant exercises significant authority," is not a "*predicate* for inferior officer status," *id.* at 1182-83 (emphases added). The Tenth Circuit thus refused to repeat the D.C. Circuit's mistakes in "mak[ing] final decision-making authority the *sine qua non* of inferior Officer status," and failing to perform a *complete* Appointments Clause analysis. *Id.* at 1189 (Briscoe, J., concurring).

Bandimere squarely rejected, too, the D.C. Circuit's interpretation of *Freytag*'s holding—established in *Landry* and reaffirmed in this case. "[P]roperly read," the Tenth Circuit concluded, "*Freytag* did not place 'exceptional stress' on final decision-making power." 844 F.3d at 1183. Indeed, properly read, *Freytag* said the opposite—that "STJs are inferior officers even though 'the ultimate decisional authority in cases under section 7443A(b)(4) rests with the Tax Court judges.'" *Id.* at 1182 (citation omitted) (discussing 26 U.S.C. § 7443A(b)(4)). *Bandimere* explained that *Freytag*'s discussion of STJs' final decision-making authority in certain cases "did not modify or supplant its holding that STJs were inferior officers based on the 'significance of [their] duties and discretion.'" *Id.* at 1183 (alteration in original) (quoting *Freytag*, 501 U.S. at 881). Rather, that discussion only "reaffirm[ed]" that "the duties of the STJs are sufficiently

significant to make them inferior officers." *Id.* at 1182. Whereas the D.C. Circuit assumed that "*every* inferior officer *must* possess final decision-making power" under *Freytag*, the Tenth Circuit concluded that "*Freytag*'s holding undermines that contention." *Id.* at 1184.

Cementing its disagreement with the decision below, *Bandimere* added that *this* Court has neither "equated significant authority with final decision-making power in *Buckley*, *Freytag*, *Edmond*, or elsewhere," nor "indicated that each of the officers it has deemed inferior possesses that power." 844 F.3d at 1184. In short, the Tenth Circuit resoundingly rejected the D.C. Circuit's exclusive focus on final decision-making authority as having no footing in this Court's teachings.

b. Recognizing that the issue was "not dispositive to [its] holding because it was not dispositive to *Freytag*'s holding," *Bandimere*, 844 F.3d at 1184 n.36, the Tenth Circuit nonetheless concluded that "SEC ALJs exercise significant authority in part because their initial decisions can *and do* become final without plenary agency review," as indeed "90 percent" do, *id.* at 1180 n.25 (emphasis added). The court explained that "the agency has no duty, based on the regulation's plain language, to review an unchallenged initial decision before entering an order stating the decision is final." *Ibid.* (citing 17 C.F.R. § 201.360(d)(2)). In fact, *Bandimere* noted multiple paths for "an initial decision to become final without plenary agency review." *Id.* at 1184 n.36. In the absence of a petition for review, for example, "the agency may simply enter an order stating an initial decision is final *without engaging in any review*." *Ibid.* (emphasis added) (citing 17 C.F.R. § 201.360(d)(2)).

The Tenth Circuit added that, at any rate, under *Edmond* "[t]he SEC's power to review its ALJs does not transform them into lesser functionaries"; "[r]ather, it shows the ALJs are inferior officers subordinate to the SEC commissioners." *Bandimere*, 844 F.3d at 1188 (citing *Edmond*, 520 U.S. at 663). Judge Briscoe thus observed that, even under the D.C. Circuit's "truncated *Freytag* analysis, [*Bandimere*] correctly holds that the SEC's ALJs are inferior Officers." *Id.* at 1194 (concurring opinion).

* * *

As things stand today, SEC ALJs are Officers in the Tenth Circuit but not in the D.C. Circuit. That is an untenable state of affairs given that Congress has authorized review of SEC final decisions *either* in the D.C. Circuit *or* in the regional circuit encompassing the petitioner's residence or principal place of business. 15 U.S.C. § 78y(a)(1). The SEC itself has acknowledged that the situation is unsustainable, staying all administrative proceedings that are appealable to the Tenth Circuit. Order, *In re Pending Administrative Proceedings*, Securities Act Release No. 10,365 (May 22, 2017). The Commission, courts, and parties to SEC proceedings all need to know sooner rather than later whether or not SEC ALJs are Officers who must be appointed pursuant to the Appointments Clause.

III. This Case Is The Ideal Vehicle To Resolve The Question Presented

This case cleanly presents the important and recurring question whether SEC ALJs are Officers of the United States. There are no potential vehicle problems.

The Judiciary has a "strong interest ... in maintaining the constitutional plan of separation of powers." *Freytag*, 501 U.S. at 879 (quoting *Glidden Co.* v. *Zdanok*, 370 U.S. 530, 536 (1962)). That interest is especially strong in the context of the Appointments Clause, which is "among the significant structural safeguards of the constitutional scheme." *Edmond*, 520 U.S. at 659. So important are the "structural" interests implicated by an Appointments Clause challenge that they can "be considered on appeal whether or not they were ruled upon below." *Freytag*, 501 U.S. at 878-79. Because these important structural interests warrant review even where such a challenge has been waived, *see id.* at 879-80, they manifestly warrant review here, where the issue was properly presented in and actually decided by both the agency and the reviewing court.

In part because of the changes wrought by the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act, the Commission has dramatically increased both the number and proportion of enforcement actions brought in administrative hearings before its ALJs. In 2014, for example, "[t]he SEC brought more than four out of five of its enforcement actions" before its ALJs, "up from less than half of them a decade earlier." Jean Eaglesham, *SEC Wins With In-House Judges*, Wall. St. J. (May 6, 2015). Moreover, the Commission agrees that SEC ALJs' fact-finding and credibility determinations are "a matter of considerable importance" to the Commission's ability to undertake review. Pet. App. 241a. The constitutionality of proceedings before SEC ALJs thus is important to the functioning of the Commission's decision-making apparatus—as well as to the rights of individuals and entities compelled to defend themselves in administrative hearings.

The question presented is also tightly focused. It is undisputed that the five SEC ALJs are not appointed by the President, the head of a department, or a court of law. Pet. App. 87a. It is also undisputed that the only appropriate remedy for an Appointments Clause violation here is vacatur of the challenged orders. *See Freytag*, 501 U.S. at 879; *United States* v. *L.A. Tucker Truck Lines, Inc.*, 344 U.S. 33, 38 (1952) (defect in the appointment of Officer is "an irregularity which would invalidate a resulting order"). The Commission has not argued that the Appointments Clause violation could be excused under a harmless-error, ratification, *de facto* officer, or any other similar doctrine. *See* Pet. App. 9a-10a. And because this case involves a petition for review of agency action, the decision and order under review can be defended only on the grounds articulated by the agency, and the Commission cannot raise any new grounds for the first time in this Court. *See SEC* v. *Chenery Corp.*, 318 U.S. 80, 87 (1943). For example, the constitutionality of ALJ removal procedures and the status of ALJs in other agencies have never been raised by any party in this case (or in *Bandimere*) and thus these are not arguments available to the government here. *But see Bandimere*, 844 F.3d at 1199-1201 (McKay, J., dissenting) (speculating on these issues without benefit of briefing by any party); *see also Bandimere* v. *SEC*, 855 F.3d 1128, 1130-32 (10th Cir. 2017) (Lucero, J., dissenting from denial of rehearing en banc) (similar).

The constitutionality of SEC ALJs has been raised in a number of pending proceedings. Only two of those—this case and *Bandimere*—have reached appellate decisions on the merits of the Appointments Clause question. The same question has also been raised in at least 13 other cases pending in the courts of appeals and 30 proceedings pending before the

Commission. *See* Pet. App. 300a-304a. These figures will only continue to increase until this Court settles the issue. The question presented by this petition—whether SEC ALJs are Officers of the United States—admits of only one answer. This dispute will grow no more ripe, and the issue no better developed, with time. This Court should grant certiorari now, in this case.*

* * *

The SEC's regime of unaccountable adjudicators has left countless casualties on the field—not least Ray Lucia. After an unblemished career spanning forty years, Mr. Lucia has been rendered unemployable in his profession and on the verge of bankruptcy—even though his free presentations, at which no securities were offered or sold and which concededly caused no investor harm, did not remotely amount to intentional fraud. The ALJ who presided over this case imposed on him "'the securities industry equivalent of capital punishment.'" *Saad* v. *SEC*, 718 F.3d 904, 906 (D.C. Cir. 2013) (citation omitted). The Framers designed the Appointments Clause precisely to prevent such abuses of power by unaccountable officials. This Court needs to decide, now, whether SEC ALJs are Officers of the United States.

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*Although the government could petition for a writ of certiorari in *Bandimere*, this case presents a better vehicle for the resolution of the Appointments Clause issue because (unlike *Bandimere*) this case raises no potential recusal issues. The constitutional issue also was more fully briefed in this case: At the en banc stage, petitioners and the government filed replacement briefs devoted solely to the Appointments Clause issue, and six *amicus* briefs were filed supporting petitioners.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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July 21, 2017

APPENDIX

APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 15-1345 **September Term, 2016**

SEC-3-15006

Filed On: June 26, 2017

Raymond J. Lucia Companies, Inc. and Raymond J. Lucia,

Petitioners

v.

Securities and Exchange Commission,

Respondent

BEFORE: Garland, Chief Judge,* and Henderson, Rogers, Tatel, Brown, Griffith, Kavanaugh, Srinivasan, Millett, Pillard, and Wilkins, Circuit Judges

JUDGMENT

This cause came on to be heard on the petition for review of an order of the Securities & Exchange Commission and was argued by counsel. On consideration thereof, it is

* Chief Judge Garland did not participate in this matter.

ORDERED and **ADJUDGED** that the petition for review is denied by an equally divided court. See D.C. Cir. Rule 35(d).

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/

Deputy Clerk

APPENDIX B

UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Argued May 13, 2016 Decided August 9, 2016

No. 15-1345

RAYMOND J. LUCIA COMPANIES, INC. AND RAYMOND J. LUCIA,
PETITIONERS

V.

SECURITIES AND EXCHANGE COMMISSION,
RESPONDENT

On Petition for Review of an Order of the Securities & Exchange Commission

* * *

Before: ROGERS, PILLARD and WILKINS, *Circuit Judges*.

Opinion for the Court by *Circuit Judge* ROGERS.

ROGERS, *Circuit Judge*: Raymond J. Lucia and Raymond J. Lucia Companies, Inc., petition for review of the decision of the Securities and Exchange Commission imposing sanctions for violations of the Investment Advisers Act of 1940 and the rule against misleading advertising. Upon granting a petition for review of an initial decision by an administrative law judge ("ALJ"), the Commission rejected petitioners'

challenges to the liability and sanctions determinations and petitioners' argument that the administrative hearing was an unconstitutional procedure because the administrative law judge who heard the enforcement action was unconstitutionally appointed. Petitioners now renew these arguments, including that the judge was a constitutional Officer who must be appointed pursuant to the Appointments Clause, U.S. CONST. art. II, § 2, cl. 2. For the following reasons, we deny the petition for review.

I.

In the Securities Exchange Act of 1934, Congress determined that transactions in securities conducted over exchanges and over-the-counter markets were "affected with a national public interest which makes it necessary to provide for regulation and control of such transactions and of practices and matters related thereto." 15 U.S.C. § 78b. To carry out the regulation of the securities markets, Congress established the Securities and Exchange Commission, to be composed of five commissioners appointed by the President with the advice and consent of the Senate. *Id.* § 78d(a). Over time Congress expanded the responsibilities of the Commission, and by 1960 it was administering six statutes, *see* 1962 U.S.C.C.A.N. 2150, 2156, including the Investment Advisers Act of 1940, 15 U.S.C. § 80b-21. In 1961, pursuant the Reorganization Act of 1949, Pub. L. No. 81-109, ch. 226, 63 Stat. 203 (now codified as amended at 5 U.S.C. §§ 901–912), the President sent Congress a proposal to allow the Commission to delegate some of its responsibilities to divisions and individuals within the Commission. *See* 1961 U.S.C.C.A.N. 1351, 1351–52. The proposal was designed to provide "for greater flexibility in the han-

dling of the business before the Commission, permitting its disposition at different levels so as better to promote its efficient dispatch." *Id.* at 1351. Further, this ability to delegate tasks would "relieve the Commissioners from the necessity of dealing with many matters of lesser importance and thus conserve their time for the consideration of major matters of policy and planning." *Id.*

In response, Congress enacted "An Act to Authorize the Securities and Exchange Commission to Delegate Certain Functions," Pub L. No. 87-592, 76 Stat. 394, 394–95 (1962). Congress made three main changes to the President's proposal: a single Commissioner's vote was sufficient to require Commission review, the authority to delegate did not extend to the Commission's rulemaking authority, and in certain instances review was mandatory for adversely affected parties in circumstances not at issue here. *Compare* 1961 U.S.C.C.A.N. at 1352, *with* 76 Stat. at 394–95. Except for modification of when Commission review is mandatory, *see* An Act to Amend the Securities and Exchange Act of 1934, Pub. L. No. 94-29, § 25, 89 Stat. 97, 163 (1975), and substitution of "administrative law judge" for "hearing examiner, *see* Pub. L. No. 95-251, § 2(a)(4), 92 Stat. 183, 183 (1978), the current version of the statute, codified at 15 U.S.C. § 78d-1, has not been amended in any material respect since its enactment in 1962, *see* Securities and Exchange Commission Authorization Act of 1987, Pub. L. No. 100-181, § 308, 101 Stat. 1249, 1254–55.

Section 78d-1 has three basic parts. Subsection (a) provides that "the Securities and Exchange Commission shall have the authority to delegate, by published order or rule, any of its functions to a division of the Commission, an individual Commissioner, an

[ALJ], or an employee or employee board, including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter." 15 U.S.C. § 78d-1(a). Subsection (b) provides that the "Commission shall retain a discretionary right to review the [delegated] action . . . upon its own initiative or upon petition of a party to or intervenor in such action." *Id.* § 78d-1(b). It also lists when Commission review of a petition is mandatory. *Id.* Subsection (c) provides:

> If the [Commission's] right to exercise such review is declined, or if no such review is sought within the time stated in the rules promulgated by the Commission, then the action of any such division of the Commission, individual Commissioner, [ALJ], employee, or employee board, shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission.

Id. § 78d-1(c).

The Commission has authority to pursue alleged violators of the securities laws by filing a civil suit in the federal district court or by instituting a civil administrative action. *See* 15 U.S.C. §§ 78u, 78u-2, 78u-3, 78v; *see also id.* §§ 77h-1, 77t(b), 80b-9. By rule, the Commission has delegated to its ALJs authority to conduct administrative hearings, 17 C.F.R. § 200.30-9, and "[t]o make an initial decision in any proceeding at which the [ALJ] presides in which a hearing is required to be conducted in conformity with the [Administrative Procedure Act ("APA")] (5 U.S.C. 557)," *id.* § 200.30-9(a); *see id.* §§ 200.14, 201.111. The ALJs have authority to, among other things, administer oaths, issue subpoenas, rule on offers of proof, examine witnesses, rule upon motions, *id.* §§ 200.14,

201.111, enter orders of default, *see id.* § 201.155, and punish contemptuous conduct by excluding a contemptuous person from a hearing, *see id.* § 201.180(a); on the other hand, they lack authority to seek court enforcement of subpoenas and have no authority to punish disobedience of discovery orders or other orders with contempt sanctions of fine or imprisonment.

In any event, the Commission retains discretion to review an ALJ's initial decision either on its own initiative or upon a petition for review filed by a party or aggrieved person. 15 U.S.C. § 78d-1(b); *see also* 17 C.F.R. § 201.411(b)–(c). Other than where a petition for review triggers mandatory review, 15 U.S.C. § 78d-1(b); *see also* 17 C.F.R. § 201.411(b)(1), the Commission may deny review, 17 C.F.R. § 201.411(b)(2). By rule, the Commission has established time limits for filing a petition for review, *id.* §§ 201.360(b), 201.410(b), and, when no petition is filed, for ordering review on its own initiative, *id.* § 201.411(c). Further, by rule, the Commission has established a procedure for finalizing its decisions. *Id.* § 201.360(d). If no review of the initial decision is sought or ordered upon the Commission's own initiative, then the Commission will issue an order advising that it has declined review and specifying the "date on which sanctions, if any, take effect"; notice of the order will be published in the Commission's docket and on its website. *Id.* § 201.360(d)(2). Thus, by rule, the initial "decision becomes final upon issuance of the order," *id.*, and then because review has been declined, by statute "the action of" the ALJ, in the initial decision, "shall . . . be deemed the action of the Commission." 15 U.S.C. § 78d-1(c).

Here, the Commission instituted an administrative enforcement action against petitioners for alleged

violations of anti-fraud provisions of the Investment Advisers Act based on how they presented their "Buckets of Money" retirement wealth-management strategy to prospective clients.[1] It ordered an ALJ to conduct a public hearing, *Raymond J. Lucia Cos., Inc.*, Exchange Act Release No. 67781, 2012 WL 3838150 (Sep. 5, 2012), and thereafter an ALJ issued an initial decision finding liability based only on one of the four charged misrepresentations and imposing sanctions, including a lifetime industry bar of Raymond J. Lucia, *Raymond J. Lucia Cos., Inc.*, Initial Decision Release No. 495, 2013 WL 3379719 (July 8, 2013). A month later, the ALJ issued an order on petitioners' motion to correct manifest errors of fact. *Raymond J. Lucia Cos., Inc.*, Administrative Proceedings Rulings Release No. 780 (Aug. 7, 2013). The Commission, *sua sponte*, remanded the case for further findings of fact on the three charges the ALJ had not addressed. The ALJ subsequently issued a revised initial decision. *Raymond J. Lucia Cos., Inc.*, Initial Decision Release No. 540, 2013 WL 6384274 (Dec. 6, 2013) ("initial decision"). Thereafter, the Commission granted petitioners' petition for review and the Enforcement Division's cross-petition for review.

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[1] Sections 206(1), (2), and (4) of the Investment Advisors Act provides that an investment adviser may not (1) "employ any device, scheme, or artifice to defraud any . . . prospective client," (2) "engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any . . . prospective client," or (4) "engage in any act, practice, or course of business which is fraudulent, deceptive, or manipulative." 15 U.S.C. § 80b-6(1), (2), (4). Under Commission Rule 206(4)-1(a)(5) an investment adviser may not "publish, circulate, or distribute any advertisement . . . [w]hich contains any untrue statement of a material fact, or which is otherwise false or misleading." 17 C.F.R. § 275.206(4)-1(a)(5).

"[O]n an independent review of the record," except as to unchallenged factual findings, the Commission found that petitioners committed anti-fraud violations and imposed the same sanctions as the ALJ. *Raymond J. Lucia Cos., Inc.*, Exchange Act Release No. 75837, at 3, 2015 WL 5172953 (Sept. 3, 2015) ("*Decision*"). The Commission also rejected petitioners' argument that the administrative proceeding was unconstitutional because the presiding ALJ was not appointed in accordance with the Appointments Clause under Article II, Section 2, Clause 2 of the Constitution. *Id.* at 28–33. Relying on *Landry v. FDIC*, 204 F.3d 1125 (D.C. Cir. 2000), the Commission concluded its ALJs are employees, not Officers, and their appointment is not covered by the Clause. *Decision* at 28–33.

II.

Petitioners first contend that the Commission's decision and order under review should be vacated because the ALJ rendering the initial decision was a constitutional Officer who was not appointed pursuant to the Appointments Clause. Because the government does not maintain that the Commission's decision can be upheld if the presiding ALJ was unconstitutionally appointed, we address this issue first because were petitioners to prevail there would be no need to reach their challenges to the liability and sanction determinations. The Commission has acknowledged the ALJ was not appointed as the Clause requires, and the government does not argue harmless error would apply. *See Ryder v. United States*, 515 U.S. 177, 186 (1995). Thus, if the court concludes, upon considering the constitutional issue *de novo*, *see J.J. Cassone Bakery, Inc. v. NLRB*, 554 F.3d 1041, 1044 (D.C. Cir. 2009), that Commission ALJs are Officers within the meaning of

the Appointments Clause, then the ALJ in petitioners' case was unconstitutionally appointed and the court must grant the petition for review.

The Appointments Clause provides that the President:

> shall nominate, and by and with the Advice and Consent of the Senate, shall appoint . . . Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

U.S. CONST. art. II, § 2, cl. 2. Unless provided for elsewhere in the Constitution, "all Officers of the United States are to be appointed in accordance with the Clause." *Buckley v. Valeo*, 424 U.S. 1, 132 (1976). This includes not only executive Officers, but judicial Officers and those of administrative agencies. *See id.* at 132–33. Only those deemed to be employees or other "'lesser functionaries' need not be selected in compliance with the strict requirements of Article II." *Freytag v. Comm'r, Internal Revenue*, 501 U.S. 868, 880 (1991) (quoting *Buckley*, 424 U.S. at 126 n.162). The Clause's limitations are not mere formalities, but have been understood to be "among the significant structural safeguards of the constitutional scheme." *Edmond v. United States*, 520 U.S. 651, 659 (1997). The Clause addresses concerns about diffusion of the appointment power and ensures "that those who wielded it were accountable to political force and the will of the people." *Freytag*, 501 U.S. at 883–84; *see also Ryder*, 515 U.S. at 182.

The Supreme Court has explained that generally an appointee is an Officer, and not an employee who falls beyond the reach of the Clause, if the appointee exercises "significant authority pursuant to the laws of the United States." *Buckley*, 424 U.S. at 126. In that case, the Court held that insofar as the Federal Election Commission ("FEC") had rulemaking authority, primary responsibility for conducting civil litigation, and power to determine eligibility for federal matching funds and federal elective office, only "Officers of the United States" duly appointed in accordance with the Appointments Clause could exercise such powers because each represented "the performance of a significant governmental duty exercised pursuant to a public law"; the commissioners had not been appointed properly and therefore could not. *Buckley*, 424 U.S. at 140–41. So too, in *Freytag*, 501 U.S. 868, where the Court considered the powers and duties of special trial judges, *id.* at 882, who as members of an Article I court could exercise the judicial power of the United States, *id.* at 888–89, to be significant and explained that an appointee is no less an Officer because some of his duties are those of an employee. For that reason, when evaluating whether an appointee is a constitutional Officer, a reviewing court will look not only to the authority exercised in a petitioner's case but to all of that appointee's duties, or at least those called to the court's attention. *See Tucker v. Comm'r, Internal Revenue*, 676 F.3d 1129, 1132 (D.C. Cir. 2012) (citing *Freytag*, 501 U.S. at 882); *Landry*, 204 F.3d at 1131–32.

This court has elaborated on what constitutes an exercise of "significant authority." Once the appointee meets the threshold requirement that the relevant position was "established by Law" and the position's "duties, salary, and means of appointment" are specified

by statute, *Landry*, 204 F.3d at 1133–34 (quoting *Freytag*, 501 U.S. at 881), "the main criteria for drawing the line between inferior Officers and employees not covered by the Clause are (1) the significance of the matters resolved by the officials, (2) the discretion they exercise in reaching their decisions, and (3) the finality of those decisions," *Tucker*, 676 F.3d at 1133; *see Landry*, 204 F.3d at 1133–34. In *Landry*, 204 F.3d at 1134, the court held that the ALJs of the Federal Deposit Insurance Corporation ("FDIC") were not Officers because they did not satisfy the third criterion; unlike the special tax judges in *Freytag*, the FDIC ALJs could not issue final decisions because their authority was limited by FDIC regulations to recommending decisions that the FDIC Board of Directors might issue, *id.* at 1133 (citing 12 C.F.R. § 308.38). This court understood that it "was critical to the Court's decision" in *Freytag* that the special trial judge had authority to issue final decisions in at least some cases, because it would have been "unnecessary" for the Court to consider whether the tax judges had final decision-making power when the judge in Freytag's case exercised no such power. *Id.* (citing *Freytag*, 501 U.S. at 882). Similarly, in *Tucker*, 676 F.3d at 1134, the court held that an employee of the IRS Office of Appeals was not an Officer because regulatory and other constraints — such as detailed guidelines, consultation requirements, and supervision — meant that Appeals employees lacked the discretion required by the second criterion. In both cases, either due to the lack of final decision power or discretion, the appointee could not be said to have been delegated sovereign authority or to have the power to bind third parties, or the government itself, for the public bene-

fit. *See Officers of the United States Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73, 87 (2007).

Landry, of course, did not resolve the constitutional status of ALJs for all agencies. *See Landry*, 204 F.3d at 1133–34; *see also Free Enterprise Fund v. Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 507 n.10 (2010). But to the extent petitioners contend that the approach required by *Landry* is inconsistent with *Freytag* or other Supreme Court precedent, this court has rejected that argument and *Landry* is the law of the circuit, *see LaShawn A. v. Barry*, 87 F.3d 1389, 1395 (D.C. Cir. 1996). For the same reason, the court must reject petitioners' view, relying on *Edmond*, that the ability to "render a final decision on behalf of the United States," while having a bearing on the dividing line between principal and inferior Officers, is irrelevant to the distinction between inferior Officers and employees. Petrs. Br. 25 (quoting *Edmond*, 520 U.S. at 665–66). Moreover, in *Edmond*, 520 U.S. at 656, the Court noted that the government did not dispute that military court appellate judges were Officers and addressed only what type of Officer they were; it had no occasion to address the differences between employees and Officers.

As to the petitioners' contentions about *Landry*'s application to Commission ALJs, the parties principally disagree about whether Commission ALJs issue final decisions of the Commission. Our analysis begins, and ends, there.

Petitioners emphasize the requirement in section 78d-1(c) that the ALJ's "action," when not reviewed by the Commission, "*shall*, for all purposes, including appeal or review thereof, *be deemed* the action of the Commission." (emphasis as added in Petrs. Br. 36).

In their view, the statute contemplates that the ALJ's initial decision becomes final in at least some circumstances when Commission review is declined. "At a minimum," they suggest, "Congress has indisputably *permitted* the [Commission] to treat unappealed ALJ decisions as final." Petrs. Br. 36–37.

The government acknowledges that the statute might have permitted this approach, but emphasizes that subsection (c) of the statute cannot be looked at in isolation because the same statutory provision on which petitioners rely also authorizes the Commission to establish its delegation and review scheme by rule. 15 U.S.C. § 78d-1(a)–(b). There can be no serious question that Section 78d-1(b) reserves to the Commission "a discretionary right to review the action of any" ALJ as it sees fit. And the Commission promulgated rules to govern that review pursuant to its general rulemaking authority under the security laws. *See Decision* at 31 n.109 (citing 17 C.F.R. § 201.360(d)(2)); *see also* 15 U.S.C. § 78w(a)(1). For the purposes of the Appointments Clause, the Commission's regulations on the scope of its ALJ's authority are no less controlling than the FDIC regulations to which this court looked in *Landry*, 204 F.3d at 1133 (citing 12 C.F.R. §§ 308.38, 308.40(a), (c)).

So understood, the Commission *could* have chosen to adopt regulations whereby an ALJ's initial decision would be deemed a final decision of the Commission upon the expiration of a review period, without any additional Commission action. But that is not what the Commission has done. Instead, by rule the Commission, as relevant, has defined when its "right to exercise [Section 78d-1(b)] review is declined" and has established the process by which an initial decision can become final and thereby "be deemed the action of

the Commission," 15 U.S.C. § 78d-1(c). First, it has afforded itself additional time to determine whether it wishes to order review even when no petition for review is filed. 17 C.F.R. § 201.411(c). Second, upon deciding not to order review, the Commission issues an order stating that it has decided not to review the initial decision and setting the date when the sanctions, if any, take effect. *Id.* § 201.360(d)(2).

Although petitioners maintain that the finality order cannot transform the ALJ's initial decision into a mere recommendation because the "confirmatory order is a ministerial formality, akin to a court clerk's automatic issuance of the mandate after the time for seeking appellate review has expired," Petrs. Br. 36, the Commission has explained that the order plays a more critical role. Until the Commission determines not to order review, within the time allowed by its rules, *see e.g.*, 17 C.F.R. §§ 201.360(d)(2), 201.411(c), there is no final decision that can "be deemed the action of the Commission," 15 U.S.C. § 78d-1(c). As the Commission has emphasized, the initial decision becomes final when, and only when, the Commission issues the finality order, and not before then. *See Decision* at 31. Thus, the Commission must affirmatively act — by issuing the order — in every case. The Commission's final action is either in the form of a new decision after *de novo* review or, by declining to grant or order review, its embrace of the ALJ's initial decision as its own. In either event, the Commission has retained full decision-making powers, and the mere passage of time is not enough to establish finality. And even when there is not full review by the Commission, it is the act of issuing the finality order that makes the initial decision the action of the Commission within the meaning of the delegation statute. Indeed, as this court observed in *Jarkesy v. SEC*, 803 F.3d 9,

12–13 (D.C. Cir. 2015) (citing 17 C.F.R. §§ 201.360(d)(2), 201.411(a)), in holding that exhaustion of constitutional issues was required, the Commission alone issues final orders.

Put otherwise, the Commission's ALJs neither have been delegated sovereign authority to act independently of the Commission nor, by other means established by Congress, do they have the power to bind third parties, or the government itself, for the public benefit. *See* 31 Op. OLC at 87. The Commission's right of discretionary review under Section 78d-1(b) and adoption of its regulatory scheme for delegation pursuant to Section 78d-1(c) ensure that the politically accountable Commissioners have determined that an ALJ's initial decision is to be the final action of the Commission.

Petitioners object generally to this understanding of the Commission's delegation scheme, but it cannot seriously be argued that the Commission's regulatory scheme is not a reasonable interpretation of the statute, specifically defining the circumstances under which its "right to exercise . . . review is declined," 15 U.S.C. § 78d-1(c), and that the Commission's interpretation of the finality order is a reasonable interpretation of its regulations. *See Christopher SmithKline Beecham Corp.*, 132 S. Ct. 156, 2165–66 (2012). Further, nothing in the legislative history of Section 78d-1, the regulatory history of 17 C.F.R. § 201.360(d), or Commission precedent indicates Congress or the Commission intended that the ALJ who presides at an enforcement proceedings be delegated the sovereign power of the Commission to make the final decision. This is consistent with Congress's adoption of the President's reorganization proposal to provide "for

greater flexibility in the handling of the business before the Commission," and "relieve the Commissioners from the necessity of dealing with many matters of lesser importance and thus conserve their time for the consideration of major matters of policy and planning." 1961 U.S.C.C.A.N. at 1351. The history of the Commission's finality regulation, 17 C.F.R. § 201.360(d)(2), demonstrates that the finality order was and remains an after-the-fact statement to the parties that the Commission has declined to order review. *See* 17 C.F.R. § 201.360(d)(1) (1995); Proposed Amendments to the Rules of Practice and Related Provisions, Exchange Act Release No. 34-48832, 2003 WL 22827684, at *12 (Nov. 23, 2003). And the Commission's precedent in *Alchemy Ventures, Inc.*, Release No. 70708, 2013 WL 6173809 (Oct. 17, 2013); *see* Petrs. Br. 32 n.5, resolved an ambiguity, ruling that even in cases of defaults ALJs must issue initial decisions as required by Commission rules; it left enforceable outstanding default orders but made clear that ALJs do not have authority to proceed without issuing initial decisions. *Id.* at *2–4 (citing 17 C.F.R. § 201.360(d)).

Because the Commission has reasonably interpreted its regulatory regime to mean that no initial decision of its ALJs is independently final, such initial decisions are no more final than the recommended decisions issued by FDIC ALJs. This is so even though the FDIC's regulations limit its ALJs to issuing "recommended decisions" and require the FDIC to consider and decide every case, whereas the Commission can choose not to order or grant full review of a case. Based on the Commission's interpretation of its delegation scheme, the difference between the FDIC's recommended decisions and the Commission's initial decisions is "illusory." Resp't. Br. 28. As discussed, the

Commission can always grant review on its own initiative, and so it must consider every initial decision, including those in which it does not order review. 15 U.S.C. § 78d-1(b); 17 C.F.R. §§ 201.360(d)(2), 201.411(c). It gives itself time to decide whether to order review and must always issue a finality order to indicate whether it has declined review. 17 C.F.R. §§ 201.360(d)(2), 201.411(c). Petitioners offer neither reason to understand the finality order to be merely a rubber stamp, nor evidence that initial decisions of which the Commission does not order full review receive no substantive consideration as part of this process. That is, petitioners have not substantiated that a finality order is just like a clerk automatically issuing a mandate, Petrs. Br. 36, and, in so asserting, have ignored that clerks have no authority to review orders or decline to issue mandates. It is also worth noting that the differences between the two regimes are not as stark as petitioners suggest. In either the FDIC or Commission system, issues of law and fact can go unreviewed; the FDIC's regulations do not require the Board to consider issues of fact and law unless a party raises the issue before the Board (after having raised it before an ALJ), *see* 12 C.F.R. § 308.40(c)(1); *see also id.* § 308.39(b)(2).

In a further attempt to distinguish the FDIC regime considered in *Landry*, petitioners contend that even if Commission ALJs do not issue final decisions, they still exercise greater authority than FDIC ALJs in view of differences in the scope of review of the ALJ's decisions. But the Commission's scope of review is no more deferential than that of the FDIC Board. It reviews an ALJ's decision *de novo* and "may affirm, reverse, modify, [or] set aside" the initial decision, "in whole or in part," and it "may make any findings or conclusions that in its judgment are proper and on the

basis of the record." 17 C.F.R. § 201.411(a). It "ultimately controls the record for review and decides what is in the record." *Decision* at 31. It may "remand for further proceedings," 17 C.F.R. § 201.411(a), as it did in petitioners' case, "remand . . . for the taking of additional evidence," or "hear additional evidence" itself. *Id.* § 201.452. Furthermore, if "a majority of participating Commissioners do not agree to a disposition on the merits, the initial decision shall be of no effect." *Id.* § 201.411(f). To the same extent the Commission may sometimes defer to the credibility determinations of its ALJs, *see, e.g.*, *Clawson*, Exchange Act Release No. 48143, 2003 WL 21539920, at *2 (July 9, 2003), so too may the FDIC, *see Landry*, 1999 WL 440608, at *23 (May 25, 1999). The FDIC and the Commission may defer to credibility determinations where the record provides no basis for disturbing the finding, but an agency is not required to adopt the credibility determinations of an ALJ, *see Kay v. FCC*, 396 F.3d 1184, 1189 (D.C. Cir. 2005) (citing 5 U.S.C. § 557(b)). By contrast, the Tax Court in *Freytag* was "required to defer" to the special trial judge's "factual and credibility findings unless they were clearly erroneous," *Landry*, 204 F.3d at 1133. Petitioners' reliance on 17 C.F.R. § 201.411(b)(2)(ii)(A) is misplaced; that rule refers to the criteria the Commission considers in deciding whether to grant a petition for review, not the subsequent proceedings, *see* 17 C.F.R. § 201.411(a), and not the Commission's determination of whether to order *sua sponte* review, *see id.* § 201.411(c).

Contrary to petitioners' suggestion, the Commission's treatment of a Commission ALJ's initial decision is not inconsistent with the treatment given to initial decisions in the APA, which provides where an agency does not exercise its authority of review, the ALJ's initial decision "becomes the decision of the

agency without further proceedings." 5 U.S.C. § 557(b); *see also* U.S. Dep't of Justice, *Attorney General's Manual on the Administrative Procedure Act* 82–83 (1947). As discussed, an initial decision is "deemed to be the decision of the Commission" but only after that decision has been embraced by the Commissioners as their own. Even though the APA may permit agencies to establish different processes, whereby an ALJ's initial decision can become final and binding on third parties, the Commission was not required to do so. Congress considered and rejected proposals to transfer final decision-making authority from agency officials to presidentially appointed judges in a separate administrative court with powers similar to those generally vested in Article I courts. *See* H.R. Rep. No. 79-1980, at 8 (1946), *reprinted in Legislative History of Administrative Procedure Act*, at 242 (1946). It determined hearing examiners (now ALJs) should continue to be located within each agency and should have independence within the Civil Service System with regard to tenure and compensation. *See Ramspeck v. Federal Trial Exam'rs Conference*, 345 U.S. 128, 132 & n.2 (1953). But that independence did not mean they were unaccountable to the agency for which they are working. The *Attorney General's Manual on the Administrative Procedure Act* 83, explained Congress envisioned that notwithstanding an ALJ's initial decision, the agency could retain "complete freedom of decision." As a contemporaneous interpretation, the Manual is given "considerable weight." *Brock v. Cathedral Bluffs Shale Oil Co.*, 796 F.2d 533, 537 (D.C. Cir. 1986) (quoting *Pacific Gas & Elec. Co. v. FPC*, 506 F.2d 33, 38 n.17 (D.C. Cir. 1974) (noting active role played by the Attorney General in the formation and implementation of the APA)). The APA provides, thus, that on appeal from

or review of the initial decision, the agency "has all the powers which it would have in making the initial decision," and even on questions of fact, *Kay*, 396 F.3d at 1189 (quoting 5 U.S.C. § 557). "an agency reviewing an ALJ decision is not in a position analogous to a court of appeals reviewing a case tried to a district court," *id.* In this way, Congress left to the agency the flexibility to have final authority in agency proceedings while providing Civil Service protections to ALJs in response to concerns their actions were influenced by a desire to curry favor with agency heads. *See Ramspeck*, 345 U.S. at 132 & n.3, 142.

Finally, petitioners point to nothing in the securities laws that suggests Congress intended that Commission ALJs be appointed as if Officers. They do point to the reference to "officers of the Commission" in 15 U.S.C. § 77u, but there is no indication Congress intended these officers to be synonymous with "Officers of the United States" under the Appointments Clause. Of course, petitioners contend that Congress was constitutionally required to make the Commission ALJs inferior Officers based on the duties they perform. But having failed to demonstrate that Commission ALJs perform such duties as would invoke that requirement, this court could not cast aside a carefully devised scheme established after years of legislative consideration and agency implementation. *See* 5 U.S.C. §§ 3105, 3313; *see also* Civil Service Reform Act of 1978, Pub. L. 95-454, 92 Stat. 1111.

III.

We turn, then, to petitioners' challenges to the Commission's liability findings and its choice of sanction, principally on the ground that punishment is being imposed for conduct that was not unlawful at the

time it occurred. They view the Enforcement Division's "entire case" to have been that petitioners misled investors by describing their presentation of how their "Buckets-of-Money" strategy would have performed historically as a "backtest" even though it was not based only on historical data and instead utilized a mix of historical data and assumptions. Petrs. Br. 45. In their view, the presentation set forth all of the assumptions that went into their backtests and so could not have been understood to have relied only on historical data.

A.

The question for the court is whether there was substantial evidence to support the Commission's determination that, by touting their investment strategy through the false promise of "backtested" historical success, petitioners violated the antifraud provisions of the Investment Advisers Act. *See Koch v. SEC*, 793 F.3d 147, 151–52 (D.C. Cir. 2015) (quoting 15 U.S.C. §§ 78y(a)(4), 80b-13(a)); *Kornman v. SEC*, 592 F.3d 173, 184 (D.C. Cir. 2010). Our review is deferential. Substantial evidence means only "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." *Koch*, 793 F.3d at 151–52 (quoting *Pierce v. Underwood*, 487 U.S. 552, 565 (1988)). The Commission's "conclusions may be set aside only if arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." *Id.* at 152 (quoting *Graham v. SEC*, 222 F.3d 994, 999–1000 (D.C. Cir. 2000)); *see also Rapoport v. SEC*, 682 F.3d 98, 103 (D.C. Cir. 2012).

The Commission found that petitioners had violated the Investment Advisers Act, *see supra* note 1, as a result of factual misrepresentations they made in

their presentations at free retirement-planning seminars. During these presentations, petitioners advocated a "Buckets-of-Money" investment strategy, which called for spreading investments among several types of assets that vary in degrees of risk and liquidity. The core benefit of the strategy, petitioners claimed, was that prospective clients could live comfortably off of their investment income while also leaving a large inheritance. During nearly forty seminars, petitioners used a slideshow to illustrate how this strategy would have performed relative to other common investment strategies. Rather than present a purely hypothetical example about how the strategy might perform, petitioners illustrated how the investment strategy would have performed for a fictional couple retiring during the historic economic downturns in the "1973/74 Grizzly Bear" market and in 1966. Each example showed that a couple using the "Buckets-of-Money" strategy would have increased the value of their investments despite the market downturns and would have done much better than those utilizing other investment strategies.

To find violations of Sections 206(1), (2), and (4) of the Investment Advisers Act, the Commission required evidence from which it could find that petitioners made statements that were misleading either because they misstated a fact or omitted a fact necessary to clarify the statement, and that those misstatements or omissions were material. *Decision* at 17; 15 U.S.C. § 80b-6(1), (2), (4). In addition, for a violation of Section 206(1), the Commission needed evidence that those statements were made with scienter. *Decision* at 17.

The Commission found that petitioners' "Buckets-of- Money" presentation was misleading for three reasons:

1. Petitioners misled prospective investors by stating that they were backtesting the "Buckets-of-Money" investment strategy. *Decision* at 17–18. The actual testing had not used only historical data and instead relied on a mix of historical data and assumptions about the inflation rate and the rate of return on one type of asset on which the strategy relied, Real Estate Investment Trusts ("REITs"). *Id.* at 17–18, 23–26. Petitioners presented their investment strategy as so effective that it would have weathered historical periods of market volatility, and nowhere suggested that they were presenting mere abstract hypotheticals. In that context, stating as "backtest" results figures that did not rely exclusively on historical data was misleading. *Id.* In addition, petitioners should not have been able to say that they backtested the "Buckets-of-Money" investment strategy when they had failed to implement what petitioners had described as a key part of the strategy: shifting (or "rebucketizing") assets from the riskiest buckets of assets to safer buckets of assets once assets in the safest buckets were spent. *Id.* at 18–19, 25. This "rebucketizing" ensured that prospective investors would never have all of their assets in the riskiest bucket.

2. Petitioners misled prospective investors by presenting the *results* that they featured in their presentations. *Id.* at 18. Petitioners represented that individuals using their "Buckets-of-Money" investment strategy starting in 1966 or 1973 would have seen the value of their investments increase. This result was based on flawed assumptions because petitioners underestimated the effect of inflation and

overestimated the expected REIT returns, thereby dramatically departing from historical reality. *See id.* Further, the failure to "rebucketize" meant that the presented result was based on an artificially high percentage of assets in stocks during the time the stock market happened to be performing well. *Id.* at 18–19. Had petitioners utilized more realistic estimates and "rebucketized," as they insisted their strategy required, they would have had to show that the "Buckets-of-Money" investment strategy had run out of assets rather than grown as advertised. *Id.* at 18.

3. Petitioners' stated result of the 1973 backtest was misleading because, even using their assumptions, the result could not be replicated and because petitioners failed to provide any documentary support for the result they presented to prospective clients. *Id.* at 17, 19. Thus, petitioners "either fabricated the 1973 backtest result or presented it to seminar attendees without ensuring its accuracy." *Id.* at 19.

The Commission also found that these misrepresentations were material because they would have been significant to a reasonable investor in determining whether to adopt the "Buckets-of-Money" investment strategy. *Id.* at 19 & n.63 (citing *Basic Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988)). In support, the Commission referenced testimony from potential investors who were present during some of the presentations. Further, because petitioners designed the slides and would have been aware of the risk of misleading prospective clients as a result of their misrepresentations, the Commission found that petitioners acted with scienter because they had been at least reckless in presenting the backtest slides. *Id.* at 19–20.

Petitioners challenge all three bases for the Commission's determination that the slides were misleading as well as the materiality of the misstatement of the 1973 results and the finding of scienter. When viewed in the context of the presentation, as a whole, petitioners maintain that there was not substantial evidence to support the Commission's finding that they misled prospective clients by stating that they had backtested the "Buckets-of-Money" investment strategy. Rather, they claim, the absence of any settled meaning of the term "backtest" meant that their use of the term, standing alone, did not necessarily imply that the "backtest" analysis would use only historical data. Such an implication was all the more remarkable, in petitioners' view, given the disclaimers on their slides stating that this particular backtest would utilize some hypothetical assumptions. Further, in their view, it was not misleading to state they had backtested the "Buckets-of-Money" investment strategy even if they had not "rebucketized" the assets in the way initially described in the strategy. Although petitioners acknowledge that they referenced "rebucketizing" in the slides, their view is that there was no evidence that "rebucketizing" was a necessary — as opposed to an optional and more advanced — component of the "Buckets-of-Money" investment strategy.

There is substantial evidence to support the Commission's finding that petitioners' "Buckets-of-Money" presentation promised to provide an historical-data-only backtest where the analysis would account for "rebucketizing." As the Commission found, experts for petitioners and the government agreed that the term backtest typically referred to the use of historical, not assumed, data. *Id.* at 17. The Commission emphasized that petitioners "introduced no expert

testimony to establish industry practice, and their own inflation and REIT experts agreed that backtests use historical rates." *Id.* at 26. The Commission accorded little weight to a single mutual fund promotional brochure emphasized by petitioners because, although the brochure used the term backtest in connection with an assumed inflation rate, two other brochures used historical rates in connection with their backtests. *Id.*

Furthermore, the Commission did not rest its analysis exclusively on petitioners' use of the word "backtest" or the Commission's understanding that the term meant an historical-data-only analysis. In response to petitioners' argument that it would be unfair for the Commission to apply a newly established definition to find petitioners conduct unlawful, the Commission explained that it was not attempting to define "backtest" for all purposes. *Id.* at 25. Rather, what was misleading was the statement to seminar attendees that petitioners had analyzed how the "Buckets-of-Money" investment strategy would have performed in the past. *Id.* That is, not only had petitioners used the word "backtest" in their presentations, they had also introduced both historical illustrations (1973 and 1966) by asking what would have happened had a couple used the "Buckets-of-Money" investment strategy at these times. To answer accurately how the strategy would have performed historically would require the use of historical data. Thus, it was misleading for petitioners not to inform seminar attendees that petitioners' backtest could not accurately answer that question. *Id.* And for that reason, even though the presentation contained disclaimers that some assumptions would be used in the historical backtests, the Commission concluded that petitioners had not altered "the overall impression that

[they] had performed backtests showing how the ["Buckets-of-Money" investment] strategy would have performed during the two historical periods." *Id.* at 23.

Petitioners likewise fail to undermine the Commission's finding that a slide purporting to backtest the "Buckets-of-Money" investment strategy would be understood by a reasonable investor to include "rebucketizing" of assets. *Id.* at 25. Contrary to the government's suggestion, petitioners did argue to the Commission that "rebucketizing" was not an essential part of the "Buckets-of-Money" investment strategy, *see* Petrs. Br. to Comm'n 14–15 (2014). The Commission rejected that argument and substantial evidence supports its finding that "rebucketizing" was an essential part of the "Buckets-of-Money" investment strategy so that any purported backtest of that strategy would imply that "rebucketizing" was taking place. Raymond J. Lucia acknowledged that an investor should never have one-hundred percent of his assets in stocks, and made related statements that an investor should not draw income directly from his stock portfolio, both of which would have been necessary over the period of the backtests absent "rebucketizing." *Decision* at 14. Further, when petitioners first introduced the "Buckets-of-Money" investment strategy in their presentation, a slide stated that "rebucketizing" would take place after the non-stock income buckets were exhausted as funds were used for living expenses. Because petitioners never made clear in their presentations that the historical analyses did not include "rebucketizing," and there is no evidence that the backtest must have been understood not to include "rebucketizing," the Commission's finding that "rebucketizing" was essential is supported by substantial evidence in the record.

Petitioners also fail to show that the Commission erred in finding that it was misleading for them to present results that overstated how the "Buckets-of-Money" investment strategy would have performed historically. *Id.* at 18. As the Commission found, petitioners' assumed inflation and REIT rates were [flawed] and had the effect of dramatically overstating the results of the historical analysis. *Id.* at 18–19. For example, the use of a flat 3% inflation rate understated the effect of inflation when the actual inflation rate reached double digits in the late 1970s and early 1980s. *Id.* at 18. Also, the failure to "rebucketize" had the effect of overstating gains. *Id.* at 18–19. Petitioners attempt to justify the use of assumptions generally, referencing the disclaimers in the slides, but nowhere maintain that the assumptions they chose could be expected to produce results that approximated historic performance. *Id.*

Petitioners take another tack in challenging the Commission's finding that using petitioners' flawed assumptions would not produce the 1973 backtest result represented in the slides. Here, they principally maintain that the Commission never charged the error in the 1973 backtest result and that they therefore had no notice that the erroneous result was under scrutiny. In fact, the charging document provided adequate notice. Incorporating the facts underlying the alleged violations, the charging document alleged that petitioners "failed to keep adequate records" and that the spreadsheet records they maintained failed to "duplicate the advertised investment strategy." *Raymond J. Lucia Cos., Inc.*, Exchange Act Release No. 67781, at 9. The Commission's finding that the 1973 backtest result was either "fabricated" or inaccurate was an outgrowth of this charge as it became clear there was no documentary proof of the presented 1973

backtest result. *Decision* at 8, 19. Petitioners admitted during the hearing that the spreadsheets they produced to substantiate the result were not actually used and included different assumptions than were relied upon in the 1973 backtest shown to potential investors. *Id.* They also admitted that the assumptions presented in the slides could not be used to generate documentary proof of the 1973 result because they had used a different set of assumptions. *Id.* Further, petitioners' expert repeated the analysis with this different set of assumptions and still was unable to replicate the 1973 result. *Id.* The Commission's finding that it was misleading for petitioners to present a result for which they had no support, particularly when the result overstated the success of the "Buckets-of-Money" investment strategy, is supported by substantial evidence.

Petitioners' challenge to the Commission's finding that the misstatement about the 1973 backtest result was material is no more persuasive. A statement is "material" so long as there is a "substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." *Basic Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988) (quoting *TSC Indus., Inc. v. Northway, Inc.* 426 U.S. 438, 449 (1976)). Petitioners suggest that the misrepresentation could not have been material because the 1973 result presented in the slide understated the success of using the "Buckets-of-Money" investment strategy. But this suggestion rests solely on the 1973 backtest result spreadsheet, which petitioners admitted did not serve as the basis for the 1973 backtest analysis shown in the presentation. Further, petitioners' experts provided substantial evidence to

support the Commission's finding that the slides overstated the 1973 backtest result. *Id.* at 19. The Commission had ample grounds to conclude that the reasonable investor would want to know that petitioners lacked documentary support for the number presented.

Finally, petitioners challenge the Commission's scienter finding. Under section 206(1), which prohibits an investment adviser from employing "any device, scheme, or artifice to defraud any client or prospective client," 15 U.S.C. § 80b-6(1), the Commission must find that petitioners acted with an "intent to deceive, manipulate, or defraud." *SEC v. Steadman*, 967 F.2d 636, 641 (D.C. Cir. 1992) (quoting *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 194 n.12 (1976)). "[E]xtreme recklessness may also satisfy this intent requirement." *Id.* This is "not merely a heightened form of ordinary negligence" but "an 'extreme departure from the standards of ordinary care, . . . which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it.'" *Id.* at 641–42 (quoting *Sundstrand Corp. v. Sun Chemical Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977)).

To the extent petitioners maintain the Commission could not have found that they acted with scienter by misleadingly using the term "backtest" because the term did not have a settled meaning at the time, they misunderstand the basis of the Commission's scienter determination. The finding of recklessness did not focus only on petitioners' use of the term, but also focused on petitioners' presentation of slides that promised an historically accurate view of how the "Buckets-of-Money" investment strategy would have

performed during periods of historic economic downturns. Petitioners' effort to read ambiguity into the term "backtest" misses the key point: Whether they referred to their examples as "historical views," "retrospective applications," or "backtests," the misleading impression is the same. For that reason, the Commission found that petitioners either "knew or must have known of the risk of misleading prospective clients to believe that [petitioners] had performed actual backtests." *Decision* at 20. Because they knew historical inflation rates were higher than their assumed rate, that a key asset (REITs) did not perform as assumed, and that not "rebucketizing" would lead to higher returns, petitioners faced an obvious risk of presenting misleading results. *See id.*

There is no record support for petitioners' objection that the Commission could not have found scienter because they sought advance approval of their slides by the Commission as well as by two FINRA-registered broker-dealers. They offer no record basis to undermine the Commission's finding that there was no evidence petitioners had flagged the backtest slides for review or had provided the materials necessary to engage in meaningful review. *See id.* at 27–28. Petitioners ignore the Commission's reliance on a December 12, 2003, letter from Commission staff stating that petitioners "should not assume that [the] activities not discussed in this letter are in full compliance with the federal securities law." *Id.* at 28. The record thus does not show that petitioners took good-faith steps to seek advance approval of the statements that the Commission found they must have known to be misleading.

B.

The court's review of petitioners' challenge to the Commission's choice of sanctions is especially deferential. Because Congress has entrusted to the Commissioners' expertise the responsibility to select the means of achieving the statutory policy in relation to the appropriate remedy, their judgment regarding sanctions is "entitled to the greatest weight." *Kornman*, 592 F.3d at 186 (quoting *Am. Power & Light v. SEC*, 329 U.S. 90, 112 (1946)). The Commission must explain its reasons for selecting a particular sanction but it is not required to follow "any mechanistic formula." *See id.* (citing *PAZ Sec., Inc. v. SEC*, 566 F.3d 1172, 1175 (D.C. Cir. 2009)). The court will intervene "only if the remedy chosen is unwarranted in law or is without justification in fact." *Id.* (quoting *Am. Power & Light*, 329 U.S. at 112–13).

The only sanction petitioners challenge is the imposition of the lifetime industry bar on Raymond J. Lucia, and that challenge is unpersuasive. The Commission adequately explained the reasons for concluding that it was in the public interest to bar him from associating with an investment advisor, broker, or dealer under the Investment Advisers Act, *see* 15 U.S.C. § 80b-3(f). Upon applying the factors set forth in *Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), the Commission concluded that a bar was necessary to "protect[] the trading public from further harm," having found that his misconduct was egregious and recurrent, *Decision* at 34–35 (citation omitted). He violated a fiduciary duty he owed to his prospective clients and did so repeatedly over the course of dozens of seminars. *Id.* at 35. He acted with a "high degree of scienter because he knowingly or recklessly

misled prospective clients for the purpose of increasing [the corporation's] client base and fees generated therefrom." *Id.* Further, such behavior could be expected in the future because he had violated his fiduciary duties and failed to recognize the wrongful nature of his conduct. *Id.* In the Commission's view, the steps he had taken — such as selling his assets in the corporation and withdrawing its investment advisor registration — were insufficient to show that he would not engage in similar misconduct in the future. *Id.* at 35–36. He was still seeking to serve as an on-demand public speaker, consultant, and media personality on retirement planning and other topics. *See id.* at 35–36 & n.132. Although acknowledging that he had stopped presenting the fraudulent backtest slides once the Commission informed him in 2010 of problems with the presentation and that he did not presently threaten to associate with an investment adviser, the Commission considered that these factors were outweighed by his recurrent and intentional misconduct and the "reasonable likelihood that, without a bar, [he] will again threaten the public interest by reassociating with an investment advisor, broker, or dealer." *Id.* at 35–36.

The Commission was unpersuaded that the evidence offered in mitigation lessened the gravity of his conduct or made it less likely that he would engage in such conduct in the future. *Id.* at 36–38. In its view, neither the possible financial losses he would suffer as a result of the permanent industry bar nor the absence of prior misconduct during forty years of working in the industry made his misconduct any less grave. "Here," the Commission concluded, "even without investor injury as an aggravating factor, [his] misconduct was egregious and a bar is in the public interest" inasmuch as its "public interest analysis focuses

on the welfare of investors generally and the threat one poses to investors and the markets in the future." *Id.* at 37 (internal citation and alteration omitted). With respect to the request for an alternative sanction of censure and monitoring, the Commission noted that it had no obligation to impose sanctions similar to those imposed in settled proceedings, where "the avoidance of time-and-manpower-consuming adversary proceedings[] justif[ied] accepting lesser remedies in settlement," *id.* at 38, and emphasized that the appropriate remedy "depends on the facts and circumstances presented" in each case, *see id.*

The record is thus contrary to petitioners' position that the Commission abused its discretion by failing to offer a sufficient justification for imposing the lifetime industry bar. *See Kornman*, 592 F.3d at 188; *see also Seghers v. SEC*, 548 F.3d 129, 135–36 (D.C. Cir. 2008). Undoubtedly the lifetime bar is a most serious sanction, *see Saad v. SEC*, 718 F.3d 904, 906 (D.C. Cir. 2013), and, in petitioners' view, more serious than the sanctions imposed for similar conduct in settled cases, *see* Petrs. Br. 61. The court, however, will not intervene simply because the Commission exercised its "discretion to impose a lesser sanction" in other cases, *see Kornman*, 592 F.3d at 186–88, for the "'Commission is not obligated to make its sanctions uniform,' and the court 'will not compare this sanction to those imposed in previous cases,'" *id.* at 188 (quoting *Geiger v. SEC*, 363 F.3d 481, 488 (D.C. Cir. 2004)); *see also Seghers*, 548 F.3d at 135. Indeed, the court has stated more broadly, that the Commission need not choose "the least onerous of the sanctions." *PAZ Sec.*, 566 F.3d at 1176. Here, the Commission considered the proposed alternative sanctions and determined, in its judgment, that they would not have been sufficient to protect investors. *Decision* at 37–38. In view of the

Commission's findings that he repeatedly and recklessly engaged in egregious conduct without regard to his fiduciary duty to his clients, petitioners fail to show that the Commission's sanction was unwarranted as a matter of policy or without justification in fact, or that it failed to consider adequately his evidence of mitigation.

Accordingly, we deny the petition for review.

APPENDIX C

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Release No. 75837 / September 3, 2015

INVESTMENT ADVISERS ACT OF 1940
Release No. 4190 / September 3, 2015

INVESTMENT COMPANY ACT OF 1940
Release No. 31806 / September 3, 2015

Admin. Proc. File No. 3-15006

In the Matter of
RAYMOND J. LUCIA COMPANIES, INC.
and
RAYMOND J. LUCIA, SR.

OPINION OF THE COMMISSION

CEASE-AND-DESIST PROCEEDING

INVESTMENT ADVISER PROCEEDING

INVESTMENT COMPANY PROCEEDING

Grounds for Remedial Action

Antifraud Violations

Former registered investment adviser and its owner committed securities fraud by making material misrepresentations to prospective clients about their retirement wealth management strategy. *Held*, it is in the public interest to bar the owner from associating with an investment adviser, broker, or dealer; revoke respondents' investment adviser registrations;

order respondents to cease and desist from further violations of the provisions violated; and order civil penalties of $250,000 against the investment adviser and $50,000 against the owner.

* * *

Appeal filed: December 27, 2013
Last brief received: July 13, 2015
Oral Argument: July 31, 2015

I. Introduction

Respondents have appealed, and the Division of Enforcement has cross-appealed, an initial decision finding that Raymond J. Lucia Companies, Inc. ("RJLC"), violated Sections 206(1), 206(2), and 206(4) of the Investment Advisers Act of 1940 by misleading prospective clients about its Buckets of Money ("BOM") retirement wealth management strategy, and that Raymond J. Lucia, Sr. ("Lucia" and, with RJLC, "Respondents"), aided and abetted and caused RJLC's violations.[1] In particular, the Administrative Law Judge ("ALJ") found that, at seminars Respondents conducted to pitch their BOM strategy to prospective clients, Respondents misrepresented that they had performed two backtests (one from 1966 to 2003 and another from 1973 to 1994) proving that a model portfolio following the BOM strategy during difficult historical market periods would substantially increase in value while also providing annual retirement income. Respondents' statements about the

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[1] *Raymond J. Lucia Cos., Inc.*, Initial Decision Release No. 540, 2013 WL 6384274 (Dec. 6, 2013). Lucia owned RJLC, which was registered with the Commission as an investment adviser from September 2002 through December 2011. Lucia, who was also a registered investment adviser, sold RJLC's assets in 2010 to his son, Raymond J. Lucia, Jr. RJLC is now defunct.

backtests were misleading, the ALJ found, because Respondents did not inform prospective clients that the backtests (i) used assumed inflation and Real Estate Investment Trust ("REIT") rates that did not reflect historical rates, (ii) did not deduct advisory fees, and (iii) did not actually follow the BOM strategy by "rebucketizing" (*i.e.*, reallocating assets between "buckets" of portfolio assets). The ALJ found that Respondents did not inform prospective clients that actual backtests would have shown their model portfolio exhausting its assets before the end of the backtest periods rather than substantially increasing in value.

For these violations, the ALJ barred Lucia from associating with an investment adviser, broker, or dealer; revoked RJLC's and Lucia's investment adviser registrations; ordered RJLC and Lucia to cease and desist from further violations of the Advisers Act; and imposed civil penalties of $250,000 on RJLC and $50,000 on Lucia.

The ALJ also found that RJLC did not violate, and Lucia did not aid and abet and cause a violation of, Advisers Act Rule 206(4)-1(a)(5) concerning fraudulent advertisements by investment advisers because he found that Respondents' live slideshow presentation did not qualify as an "advertisement" under that rule. The ALJ further found that RJLC did not violate Advisers Act Section 204 concerning the maintenance of records by investment advisers.[2] The Division cross-appealed only the Rule 206(4)-1(a)(5) findings.

We find that RJLC violated, and Lucia aided and

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[2] The ALJ found that Section 204 did not apply to Respondents' backtests because they did not concern the performance of specific managed accounts or specific securities recommendations.

abetted and caused RJLC's violations of, Advisers Act Sections 206(1), 206(2), and 206(4), and Rule 206(4)-1(a)(5). For these violations, we impose the same sanctions as the ALJ imposed. We base our findings on an independent review of the record, except with respect to those findings not challenged on appeal.

Finally, we reject Respondents' contention that the administrative hearing was an unconstitutional procedure because the Commission ALJ who presided over this matter was not appointed in accordance with the Appointments Clause of the U.S. Constitution.[3] As we explain below, a Commission ALJ is a "mere employee"—not an "officer"—and thus the appointment of a Commission ALJ is not covered by the Clause.

II. Facts

At the center of this proceeding is a slideshow presentation[4] that Respondents projected onto a screen at seminars to pitch their BOM strategy to prospective clients; in particular, the proceeding focuses on the slideshow's discussion of two "backtests" to prove the efficacy of Respondents' BOM strategy during difficult historical market periods. At issue is, (i) whether Respondents led prospective clients to believe that they had performed backtests, as the Division claims, or hypothetical illustrations, as Respondents claim; (ii) if the former, whether Respondents had actually performed backtests; and (iii) if Respondents had not actually performed backtests but nevertheless led prospective clients to believe that they had

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[3] *See* U.S. Const. art. II, § 2, cl. 2.

[4] Lucia has been presenting a variation of the slideshow since around 2000. Lucia used the version of the slideshow discussed herein from around 2009 to 2010.

done so, whether there is a difference between Respondents' purported backtest results and the results that actual backtests would have shown.

We begin by summarizing the undisputed facts surrounding the slideshow presentation and Respondents' calculations in support thereof. We then present the conflicting evidence regarding Respondents' assertions during that presentation, including the meaning of the term "backtest" and the parties' expert evidence on the effect that using historical inflation and REIT rates, including advisory fees, and rebucketizing would have had on Respondents' "backtest" calculations.

A. The BOM seminar presentation

The BOM strategy, which Lucia developed, generally advocates using safe portfolio assets for retirement income before depleting riskier assets, thereby giving riskier assets time to grow.[5] From approximately 2000 through 2011, Lucia pitched the BOM strategy to prospective RJLC clients at seminars across the United States.[6] As noted, Lucia used a slideshow that he projected onto a screen during his

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[5] The Division has not argued that the BOM strategy itself violates the securities laws.

[6] Lucia estimates that he presented the BOM strategy at about forty seminars per year, and to over 50,000 total seminar attendees, the purpose of which was to generate leads for RJLC. To that end, Respondents gave prospective clients response cards to complete at the seminars to indicate their interest in a complimentary financial planning consultation with an RJLC advisor. Lucia also promoted the BOM strategy on his nationally syndicated radio show, *The Ray Lucia Show*, and in three books on investing for retirement that he authored: *Buckets of Money: How to Retire in Comfort and Safety* (2004); *Ready . . . Set . . . Retire!* (2007); and *The Buckets of Money Retirement Solution: The Ultimate Guide to Income for Life* (2010).

seminar presentations.[7] The slideshow consisted of four parts:[8] (i) a general discussion of investment risks and strategies; (ii) a description of various hypothetical couples following strategies purportedly inferior to BOM; (iii) a description of the BOM strategy and how it would work for a hypothetical couple dubbed the "Bold Bucketeers"; and (iv) the 1966 and 1973 backtests at issue in this proceeding.[9]

1. The three hypothetical couples

After beginning the presentation with a lengthy discussion of various investment risks and strategies, Lucia described three hypothetical couples to illustrate problems caused by following strategies purportedly inferior to BOM. For the illustrations, each couple was assumed to have a $1 million nest egg to invest with the goals of leaving $1 million to their chil-

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[7] Lucia also used a similar version of the slideshow in pitching the BOM strategy in a video posted on RJLC's website on February 16, 2009 (the "Webinar"). The OIP does not mention the Webinar, but Respondents introduced it as evidence of what Lucia told prospective clients at the seminars.

[8] It is undisputed that Lucia was responsible for, and approved the content of, the slideshow.

[9] As noted, Respondents contend that they did not lead prospective clients to believe that they had performed backtests. But because Respondents used the word "backtest" in their seminars to describe their analysis of how the BOM strategy would have fared for a model portfolio from 1966 to 2003 and 1973 to 1994, we also use that word to describe their analysis. That word is also appropriate because, as discussed below, we find that Respondents led prospective clients to believe that they had performed backtests.

dren and producing $60,000 in annual retirement income.[10]

a. Conservative Campbells

The slideshow stated that one couple, dubbed the "Conservative Campbells," invested their $1 million nest egg in conservative investments such as CDs, bond funds, and individual bonds. Their portfolio produced a hypothetical 6% annual return but the Campbells also withdrew $60,000 per year for income (*i.e.*, 6% of the portfolio). The slideshow stated that the problem with this strategy is that, assuming 3% annual inflation, the purchasing power of the Campbells' $60,000 annual income would diminish to $44,644 in ten years, $33,221 in twenty years, and $24,719 in thirty years. As a result, if the Campbells died after thirty years, their children would inherit $1 million but with the equivalent purchasing power of $411,987 from the initial retirement date. And if the Campbells indexed their $60,000 annual income to 3% assumed inflation every six years, they would run through their nest egg within twenty-seven years.[11]

b. High Rolling Hendersons

The slideshow stated that a second couple, dubbed the "High Rolling Hendersons," invested their $1 million nest egg in stocks because they believed that,

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[10] Most slides for this portion of the presentation included disclaimers that "[t]his is a hypothetical illustration and is not representative of an actual investment."

[11] For indexing, the slideshow clarified that the couple would increase the amount they withdrew for annual income every six years assuming 3% inflation for each of the six years. Thus, the Conservative Campbells would withdraw $60,000 each year for six years, and then $71,500 each year for another six years, and so on.

since stocks average 10% in annual return, in thirty years their portfolio would be worth $4,203,320 after withdrawing $60,000 for annual inflation indexed income. But the Hendersons would have problems if they retired at the beginning of a big bear market. For example, the slideshow stated that if the Hendersons had retired on January 1, 1973, the beginning of a two-year period when the market declined by 41.13%, they would have exhausted their portfolio in seventeen years based on the performance of the S&P 500 for that period assuming that they had withdrawn $60,000 in annual income indexed by 3% annual inflation.[12]

c. Balanced Buttafuccos

The slideshow stated that a third couple, dubbed the "Balanced Buttafuccos," invested their $1 million nest egg 40% in bonds and 60% in stocks. The slides stated that the Buttafuccos have a "better more 'balanced' approach" than the Campbells and Hendersons. But when their strategy is "backtested" with a retirement date starting on January 1, 1973, the Buttafuccos are shown to have exhausted their retirement portfolio in twenty-one years. The slides stated that the "backtest" was based on the performance of the S&P 500, an assumed 6% constant bond return, and the Buttafuccos having withdrawn $60,000 annual income for the first six years, $71,500 annual income for the next six years, and $85,500 annual income for another six years.[13]

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[12] Like the Campbells, the Hendersons were assumed to have increased the amount they withdrew for income every six years assuming 3% inflation for each of the six years.

[13] Although not stated explicitly in the Buttafucco slides, the annual income for each six year period in Respondents'

2. Description of the BOM strategy

The slideshow then described how the BOM strategy would work for a fourth hypothetical couple, dubbed the "Bold Bucketeers," who also had a $1 million nest egg.[14] In following the BOM strategy, the Bold Bucketeers divided their portfolio into three "buckets" of assets: Bucket #1 held "[s]afe money in a self-depleting bucket aimed at providing income to live on for" six years (*e.g.*, CDs, T-bills, bonds); Bucket #2 held "[s]afe, or moderately safe, money aimed at replacing Bucket #1 with inflation indexed income for the next period (6 years)" (*e.g.*, bonds, fixed annuities); and Bucket #3 held "[h]igher risk money invested for long term growth potential" (*e.g.*, stocks and REITs).[15]

In illustrating the BOM strategy, the slideshow stated that Bucket #1 was assumed to have a 4% return, Bucket #2 a 5.5% return, and Bucket #3 a 10% stock return and 7.75% REIT dividend return, and that $60,000 income was indexed by an "[a]ssumed 3% inflation" every six years.[16] At the end of the initial six year period, Bucket #1 had been fully depleted for income, at which point the assets from Bucket #2 were used for income for the next six years. After twelve

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"backtest" increased assuming 3% inflation for each of the six years (*i.e.*, $60,000 with 3% annual inflation after six years equals about $71,500).

[14] Most slides for this portion of the slideshow included disclaimers that "[r]ates of return are hypothetical in nature and are for illustrative purposes only."

[15] REITs issue equity and/or debt securities to raise capital to purchase and manage income-producing real estate, such as apartment complexes, shopping centers, and office buildings.

[16] The slideshow disclaimed, inter alia, that "[i]nvesting in real estate and [REITs] involve special risk, such as: limited liquidity and demand for real property . . . ."

years, Bucket #2 had also been fully depleted for income. But the long term assets in Bucket #3 had grown to a value of $1.4 million which, the slideshow stated, was then "[r]e-[b]ucketize[d] for another 12 years."[17]

3. Backtest slides

Finally, Lucia discussed the backtests at issue here, beginning with the backtest from 1973 to 1994, and concluding with the backtest from 1966 to 2003.

a. 1973 backtest slides

The slideshow introduced the 1973 backtest by asking, "But Can Buckets Stand Up To The Test Of The '73/'74 Grizzly Bear?" The next slide, titled "Back Tested Buckets," set forth the assumptions for the backtest, including that (i) the Bold Bucketeers invested their $1 million portfolio beginning on January 1, 1973; (ii) the portfolio was 20% invested in REITs; (iii) "actual treasury rates of return" were used "to calculate fixed income/bond returns"; (iv) "actual S&P 500 returns" were used "to calculate growth returns"; and (v) the Bold Bucketeers withdrew annual income of $60,000 from 1973 to 1978, $71,500 from 1979 to 1984, $85,500 from 1985 to 1990, and $96,000 from 1991 to 1994.[18] The slideshow concluded that the Bold

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[17] "Rebucketization" meant that portions of the assets in Bucket #3 would be reallocated to Buckets #1 and #2 after their assets had been fully depleted for income.

[18] The slides did not state the inflation or REIT rates used in the 1973 backtest or whether advisory fees, such as those charged by RJLC, were factored into the 1973 backtest. Lucia testified that annual income was indexed by 3% inflation every six years for the period of 1973 to 1990, but that Respondents made an error in calculating 3% inflation indexed income for the final period of 1991 to 1994. Respondents' expert, John Hekman,

Bucketeers' portfolio would have been worth $1,544,789 by 1994, the same point in time when the Balanced Buttafuccos' portfolio would have been worth $0.[19]

b. 1966 backtest slides

The slideshow introduced the 1966 backtest by asking, "What would have happened if you retired in 1966"?[20] The slideshow then compared 1966 backtests that Respondents calculated for three different portfolios: (i) a version of the Balanced Buttafuccos' portfolio;[21] (ii) a version of the Bold Bucketeers' portfolio without REITs; and (iii) a version of the Bold Bucketeers' portfolio with REITs. The slideshow stated that, for the 1966 backtests: (i) the "examples are based on actual market returns for the period(s) listed"; (ii) "[b]ond returns are based on US Treasury returns"; (iii) "[s]tock returns are based on S&P 500 returns"; (iv) "REIT returns are based on a 7% annual return"; and (v) "[i]nflation is based at 3% annual."[22]

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calculated that 3% inflation indexed income for that period would have been $102,092, not $96,000.

[19] The slides for the 1973 backtest included a disclaimer that "[r]ates of return are hypothetical in nature and are for illustrative purposes only."

[20] In the Webinar, Lucia introduced the slides by stating that he "did a backtest" for his "friend," Ben Stein, who had asked him this question concerning how the BOM strategy would have fared during the market stagnation of 1966 to 1982, a period when the Dow Jones Industrial Average began and ended at around 1,000 points. Stein is an actor, writer, and economic commentator, who spoke at some of Respondents' seminars.

[21] The slides for the 1966 backtests did not mention the Balanced Buttafuccos, but the first portfolio backtested used the same balanced portfolio approach (60% stocks, 40% bonds).

[22] The slides did not state whether advisory fees were factored into the backtests. Also, unlike earlier slides, the 1966 backtest

For the version of the Balanced Buttafuccos' portfolio, the slideshow stated that the $1 million beginning balance was invested 60% in stocks and 40% in bonds, from which $50,000 annual income was withdrawn on a pro rata basis. The slides concluded that, by 2003, the portfolio would have been worth $30,000 with $0 remaining for annual income.

The slideshow then stated that when the BOM strategy was applied to the same $1 million portfolio invested 60% in stocks and 40% in bonds (*i.e.*, Bold Bucketeers without REITs), the $50,000 annual income was withdrawn from bonds first rather than pro rata. As a result, by 2003, the portfolio would have been worth $1.2 million with $150,000 for annual income.

Finally, the slideshow stated that when REITs were added, the $1 million portfolio following the BOM strategy became split 40% in stocks, 40% in bonds, and 20% in REITs (*i.e.*, Bold Bucketeers with REITs), and the $50,000 annual income was withdrawn from bonds and REITs first.[23] The slideshow concluded that, by 2003, the portfolio would have been worth $4.7 million with $150,000 for annual income.

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slides did not include disclaimers. But in the Webinar, Lucia stated: "[L]et's pretend that from that point forward [*i.e.*, 1966], inflation was three percent. We know it was more. But we wouldn't have known that at the time." Lucia testified that he presented the backtest assumptions the same way in the seminars and Webinar.

[23] Lucia clarified in the Webinar that income is initially drained from the REIT "dividend yield" and bonds, and that the REIT itself is liquidated at a later point for income. Lucia referred in the Webinar to the REIT investment for the 1966 backtest as "direct ownership in real estate."

B. Respondents' actual backtest calculations

1. 1973 backtest calculations

Before the hearing, Respondents produced two spreadsheets that they claimed to have used in calculating the 1966 and 1973 backtests. But during the hearing, Respondents admitted that they did not actually use the spreadsheet they produced for the 1973 backtest to perform that backtest and that the spreadsheet included some assumptions that differed from their backtest. Respondents also admitted that they have no other documentary support for the 1973 backtest.

During the hearing, Lucia also asserted that the slideshow misstated the assumptions used for the 1973 backtest.[24] Lucia testified that rather than using actual S&P 500 returns and treasury returns for the entire twenty-one year period of the 1973 backtest (as presented in the slideshow), Respondents used those returns for only the first two years and then used a flat 10% stock return and 6% bond return for the remaining years. Lucia testified that he neglected to correct the error during his seminar presentations.[25]

But using assumptions similar to those that Lucia testified Respondents actually used in performing the 1973 backtest, Respondents' expert, John Hekman,

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[24] Lucia testified that he personally "did some of the work early on" for the 1973 backtest but that it was completed by an RJLC employee.

[25] Respondents also concede that the 1973 backtest did not include advisory fees or rebucketize the stock investments after bonds and REITs were drained for income. As noted above, this information was not included in the slides for the 1973 backtest.

was unable to replicate the 1973 backtest result presented in the slideshow.[26] Hekman calculated that, by 1994, the Bold Bucketeers' portfolio would have been worth $507,194, an amount substantially lower than the $1,544,789 claimed in the slideshow. Respondents offered no evidence related to this discrepancy or otherwise explained it. It is therefore unclear how Respondents arrived at $1,544,789.

2. 1966 backtest calculations

As noted, Respondents also produced a spreadsheet that they claimed to have used in calculating the 1966 backtest. Respondents specifically used that spreadsheet in calculating the 1966 backtest of the version of the Bold Bucketeers' portfolio with REITs.[27] Respondents did not produce any documentary support for the other two 1966 backtests.[28]

The spreadsheet shows that the backtest to which

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[26] Hekman, who holds a Ph.D. in economics, is a managing director at FTI Consulting, a firm that provides consulting and expert testimony regarding financial matters. Hekman assumed a 6% bond rate, actual S&P 500 returns for the first two years, 10% stock returns for the remaining years, a 5% annual increase in REIT principal, and a REIT dividend rate ranging between approximately 6.6% and 7.76% per year. Hekman also adjusted the Bold Bucketeers' initial $60,000 annual income by 3% annual inflation every six years (*e.g.*, $60,000 for the first six years, $71,500 for the next six years, etc.), and did not deduct advisory fees or rebucketize the portfolio.

[27] RJLC's Director of Financial Planning, Richard Plum, testified that he performed the 1966 backtest calculations in 2004 at Lucia's request. Lucia testified that he designed the 1966 backtest.

[28] Plum testified that he created spreadsheets for the 1966 backtests of the Balanced Buttafuccos' portfolio and the Bold Bucketeers' portfolio without REITs, but Respondents did not produce these spreadsheets to the Division.

it was applicable used the following factors: (i) a $1 million investment beginning on January 1, 1966, split 40% in stocks, 40% in bonds, and 20% in REITs; (ii) $50,000 income withdrawn in 1966, adjusted each subsequent year by 3% inflation; (iii) actual annual S&P 500 returns as a proxy for stock returns; (iv) actual annual treasury returns as a proxy for bond returns; (v) a flat REIT principal of $200,000; and (vi) a flat 7% REIT dividend yield. During the first eleven years of the backtest, income was withdrawn from the $14,000 annual REIT dividend yield (7% on $200,000) with the remaining amount withdrawn from T-bills. At the end of the eleventh year, the $200,000 REIT principal was liquidated and reinvested in T-bills, and then from years twelve through fifteen the remainder of the T-bill investment was drained for income. Thereafter, from 1981 through 2003, the entire Bold Bucketeers' portfolio remained in stocks rather than being rebucketized. No advisory fees were factored into the backtest.[29]

C. The parties' experts agree that Respondents did not perform actual backtests.

Respondents' expert, Hekman, and the Division's expert, Steven Grenadier,[30] agreed that a backtest uses data from a specific historical period to evaluate

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[29] The spreadsheet Respondents produced as empirical evidence of the 1973 backtest used the same assumptions as the 1966 backtest spreadsheet, except that it began on January 1, 1973, rather than January 1, 1966, and assumed that an initial $60,000 rather than $50,000 was needed for annual income, with that amount adjusted each subsequent year by 3% inflation.

[30] Grenadier is a Professor of financial economics at Stanford University.

how an investment strategy would have actually performed during that period.[31] Both experts also agreed that, based on their understanding of the term, the slideshow did not present the results of actual backtests.[32] Grenadier opined that Respondents did not conduct backtests because they used assumed rather than historical inflation and REIT rates, and did not include transaction costs for implementing the BOM strategy.[33] Grenadier also concluded that, by not rebucketizing, Respondents' backtest spreadsheets "concentrate[d] assets in a manner inconsistent with the [BOM] portfolio allocation strategy as outlined in the presentation."

Nonetheless, Respondents disputed that there is an established definition of "backtest" and introduced evidence that, they claimed, showed that it is standard in the financial planning industry to use assumed rates in backtests. Lucia testified that, in the financial planning industry, backtests routinely use "not

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[31] Respondents' chief compliance officer, Theresa Ochs, also testified that a backtest needs to use accurate historical data to provide an accurate indication of how a strategy may have performed in the past.

[32] Hekman also testified that he understood from reviewing the slideshow that it did not purport to present the results of actual backtests.

[33] Respondents' other expert, Kevin T. Gannon, also testified that he would not "use a hypothetical rate of return in a backtest" because he would use actual data in a backtest. Gannon, a Certified Public Accountant, is a managing director and president of Stanger & Co., a real estate investment banking firm.

only averages, for example, inflation, but also . . . hypothetical other investment returns . . . ."[34] As an example, Respondents introduced a brochure issued by American Funds (a large mutual fund house), which used a 4% assumed inflation rate for a backtest from 1961 to 2010. Lucia testified that in addition to American Funds, "there are dozens of variable annuity companies and software companies that do the same thing."

But other than the American Funds' brochure and Lucia's testimony, Respondents did not introduce any evidence of companies using assumed rather than historical data in backtests. To the contrary, Respondents introduced into evidence brochures from Fidelity Investments and Financial Engines Income+ reporting the results of backtests that appear to have used historical stock, bond, and inflation rates.

Respondents also claimed that the American Funds brochure was an example of an industry practice not to include fees in backtests. But it is unclear from the brochure if the two backtests discussed therein included fees. The brochure does not mention fees for the first backtest but it implies that the second backtest included fees by stating that the results "are at net asset value."[35] Also, although not mentioned by Respondents as an example of industry practice con-

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[34] Plum similarly testified that the financial planning industry has always used a mixture of "historical return rates" and "hypothetical assumed annual inflation rate[s]" in backtests.

[35] "Net asset value" is "[t]he market value of a share in a mutual fund, computed by deducting any liabilities of the fund from its total assets and dividing the difference by the number of outstanding fund shares." Black's Law Dictionary 1061 (7th ed. 1999).

cerning fees, the backtest in the Financial Engines Income+ brochure discussed above included fees, and the Fidelity brochure discussed above disclosed that fees were not included in its backtest.

D. The difference between Respondents' purported backtest results and what actual backtests would have shown

The Division's expert, Grenadier, analyzed the two spreadsheets Respondents produced as empirical evidence of the 1966 and 1973 backtests.[36] He concluded that the spreadsheets "use[d] 'important and inaccurate assumptions about inflation, investment returns and liquidity, and implementation costs that significantly affect the results and produce misleading information." Grenadier reran the calculations in the spreadsheets "[s]ubstituting actual, historical data," and produced the results discussed below showing "relatively lower ending portfolio balances than what is reflected in the presentation and spreadsheets, or portfolios that are entirely depleted resulting in substantial unmet income needs." Respondents introduced evidence, including testimony from their expert witnesses, challenging some but not all of Grenadier's

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[36] While, as noted above, Respondents admitted that they mistakenly produced the 1973 backtest spreadsheet, Grenadier's analysis of it is still relevant because it contains assumptions similar to those Respondents claimed to have used in the 1973 backtest. It differs only in that it used actual S&P 500 returns and treasury returns for the length of the backtest rather than 10% stock and 6% bond returns after the first two years, and that it adjusted the amount withdrawn for income by 3% inflation each year rather than by six year increments (*i.e.*, $60,000 for the first six years, $71,500 for the next six years, etc.).

findings.[37]

1. The effect from using historical inflation rates

Grenadier found that the backtest spreadsheets were significantly impacted by using a fixed and assumed 3% inflation rate rather than historical inflation for each of the years considered because many high inflation years occurred early in the backtest periods. Grenadier found that relatively higher inflation as measured by the Consumer Price Index ("CPI"),[38] such as the double-digit inflation of the late 1970s to early 1980s, would have caused the Bold Bucketeers' portfolios to deplete their assets faster in the early years "to have withdrawals that ke[pt] up with inflation," and as a result they would have had "less portfolio later to accumulate returns to consume on."[39]

Grenadier found that by substituting annual historical inflation rates as measured by CPI-U for Respondents' fixed 3% rate, the revised 1966 backtest spreadsheet shows the BOM portfolio being "fully depleted by 1986" and the revised 1973 backtest spreadsheet shows the BOM portfolio being "fully depleted

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[37] Respondents also introduced evidence to show that their assumed 3% inflation and 7% REIT dividend rates were reasonable to use in hypothetical illustrations. But this evidence is irrelevant because, as we find below, Respondents led prospective clients to believe that they performed backtests and not hypothetical illustrations, and backtests use historical and not assumed data.

[38] CPI measures inflation and is maintained by the Bureau of Labor Statistics. Grenadier specifically used CPI-U, which is a category of CPI measuring inflation for urban consumers.

[39] CPI-U was 11.3% in 1979, 13.5% in 1980, and 10.3% in 1981. Lucia agreed that investors would have experienced double digit inflation during this period.

by 1989."[40]

Respondents' expert, Hekman, countered that CPI-U overstated inflation for two reasons. First, Hekman stated that a 1996 report issued by a commission appointed by the Senate Finance Committee (the "Boskin Commission"), and a subsequent paper issued ten years later by a former commission member (Robert Gordon), found that CPI-U had been overstating increases in the annual cost of living. Hekman stated that, based on those findings, CPI-U is "too high by an average of 1.2% per year through 1996 and 1.0% thereafter." Second, Hekman stated that "the most realistic inflation rate for retirees is one that accounts for [their] declining pattern of spending," and concluded that an additional 2% should be deducted from annual CPI-U on top of the corrections suggested by the Boskin Commission and Gordon.

Based on those downward adjustments to CPI-U, Hekman ran two recalculations of the 1966 backtest spreadsheet. In the first, Hekman found that by substituting annual CPI-U adjusted by the Boskin Commission corrections (*i.e.*, annual CPI-U minus 1.2% through 1996 and 1.0% thereafter) for Respondents' fixed 3% rate, the 1966 backtest spreadsheet shows the BOM portfolio running out of money in 1994. In the second, Hekman found that by reducing annual CPI-U by an additional 2% on top of the Boskin Commission corrections to account for reduced retiree spending and substituting that data for Respondents' 3% rate, the 1966 backtest spreadsheet shows the

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[40] Lucia testified that he does not dispute that, if historical inflation as measured by CPI-U had been used in the 1966 or 1973 backtest spreadsheets, it would have resulted in the model BOM portfolios being fully depleted before the end of the backtest periods.

BOM portfolio increasing to a value of over $6.6 million by 2003.

While Grenadier agreed that retirees over sixty-five tend to spend less money than non-retirees, he testified that "has nothing whatsoever to do with inflation." Grenadier testified that to account for any decrease in spending in the 1966 backtest spreadsheet, the assumed $50,000 per year income—and not inflation—should be decreased.

2. The effect from using historical REIT rates of return

Respondents acknowledge that, from 1966 to 1971, REITs were not readily available to investors. For this reason, Grenadier was unable to factor historical REIT returns into the 1966 backtest spreadsheet for that period. For the period after 1971, Grenadier also found it significant in analyzing both the 1966 and 1973 backtest spreadsheets, that Respondents' slideshow did not make clear whether Respondents were using assumed returns from publicly traded REITs, public non-traded REITs, or private REITs.[41]

For the first category, Grenadier found that substituting annual historical returns for publicly traded REITs as measured by the National Association of Real Estate Investment Trusts ("NAREIT") All REIT Index[42] back through 1972 into the 1966 backtest

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[41] Publicly traded REITs file with the Commission and have their shares traded on an exchange, public non-traded REITs file with the Commission but do not trade their shares on an exchange, and private REITs neither file with the Commission nor trade their shares on an exchange.

[42] NAREIT began maintaining indices of annual returns for publicly traded REITs in 1972.

spreadsheet (leaving all other data unchanged) resulted "in a total investment in REITs of only $85,646 at the time the REIT investment [was] liquidated, as compared to $200,000 in the original spreadsheet, and total assets of only $1.3 million at the end of 2003, as compared to $4.7 million in the original spreadsheet."[43] Grenadier also found that substituting such data into the 1973 backtest spreadsheet (leaving all other data unchanged) resulted "in a total investment in REITs of only $134,031 at the time the REIT investment [was] liquidated, as compared to $200,000 in the original spreadsheet, and total assets of only $2.8 million at the end of 2003, as compared to $4.1 million in the original spreadsheet."[44]

For the last two categories, Grenadier found that, to the extent Respondents were using public non-traded or private REITs, the backtest spreadsheets should have considered "the ability and potential cost to liquidate the REIT investment."[45] As noted, Respondents' 1966 backtest spreadsheet liquidated the

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[43] Gannon testified that a more reasonable index to use for historical publicly traded REIT returns is the NAREIT Equity REIT Trust Index ("NAREIT Equity Index"), which includes REITs invested only in real estate equity, because equity REITs were the subject of Respondents' backtests. Grenadier testified that he used the NAREIT All REIT Index because it was unclear whether the REIT investment in the backtests was limited to only equity or mortgage REITs. In any event, Gannon did not analyze, and it is unclear from the record, what effect substituting data from the NAREIT Equity Index into the spreadsheets would have had on the spreadsheet results.

[44] The 1973 backtest in the slideshow ended in 1994, but the 1973 backtest spreadsheet was calculated through 2003.

[45] While publicly traded REITs are highly liquid, non-traded REITs are substantially less liquid because they generally have a minimum required holding period after which redemption

$200,000 REIT principal at the end of the eleventh year after T-bills had been drained down to a level at which they could no longer cover income.[46] In doing so, Grenadier found that the spreadsheets "ignore that redemption of private and/or public non-traded REITs may be difficult and costly."

Gannon did not offer expert testimony concerning the effect on the backtests from using annual historical REIT returns.[47]

3. The effect from deducting advisory fees

Grenadier found that if a strategy has implementation costs, like BOM, it is important when backtesting the strategy to include such costs because they "may reduce, and at times eliminate, the benefits of [the] strategy." Grenadier found that, by assuming zero implementation costs, Respondents' backtest spreadsheets overstated "the ending portfolio balances." In particular, Grenadier found that the backtest spreadsheets should have included "cost[s] associated with an investment in the S&P 500 Index," T-bills, and REITs. By incorporating representative mutual fund fees on the stock portfolio into the spreadsheets (leaving all other data unchanged), Grenadier found that the value of the model portfolio dropped in the (i) 1966 backtest spreadsheet to $2.5 million from $4.7 million by 2003; and (ii) 1973 backtest spreadsheet to $3.1 million from $4.1 million

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characteristics vary by REIT. Some non-traded REITs may allow investors to redeem shares once a quarter, subject to certain requirements; others link redemption to a required liquidity event after a fixed amount of time.

[46] The 1973 backtest spreadsheet liquidated the $200,000 REIT principal at the end of the ninth year.

[47] Respondents retained Gannon to opine on the use of a hypothetical 7% REIT rate of return in hypothetical illustrations.

by 2003.[48]

Respondents offered no expert testimony on the issue of costs. And Lucia testified that he knew fees can significantly reduce a portfolio's returns over time.

4. The effect from rebucketizing

Grenadier concluded that the 1966 and 1973 backtest spreadsheets were inconsistent with the BOM strategy presented in the seminars because they did not rebucketize after T-bills and REITs had been exhausted for income and instead left all assets in stocks. Grenadier noted that for both spreadsheets, "the average S&P 500 return over the time period in which the portfolios [were] entirely invested in stocks [was] higher than the average for the time period in which the portfolios [were] also invested in other assets besides stocks." In addition, although not directly addressed by Grenadier, from the record evidence it appears that, for the period in the 1966 backtest spreadsheet that the model portfolio was entirely invested in stocks (1981 to 2003), the average S&P 500 return was substantially higher than T-bill returns and about equivalent to publicly traded REIT returns as measured by the NAREIT Equity Index. And from 1986 to 2003, when the BOM portfolio in the 1973 backtest spreadsheet was entirely invested in stocks, the average S&P 500 return was substantially higher than T-bill returns and slightly higher than publicly traded REIT returns as measured by the NAREIT Equity Index.

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[48] Grenadier used the average equity mutual fund fee of 0.8% for 1966 to 1970 and 1% for 1971 to 1977. Thereafter he used 0.05% to match the fee charged by the least expensive mutual fund (Vanguard 500 Fund) for that period.

Respondents conceded that they did not rebucketize the 1966 or 1973 backtests and offered no expert testimony to support their approach. Lucia also admitted at the hearing that the BOM strategy does not advocate that investors leave their assets in stocks after draining other assets for income,[49] and stated in the Webinar that investors (i) should not "put a hundred percent of [their] money into the stock market" and (ii) should "never drain that stock portfolio for income."[50] Lucia also testified that he was aware that if the 1966 backtest spreadsheet had been rebucketized, the model portfolio would have ended up with significantly less money.

Lucia testified, however, that seminar attendees would have known that the backtests were not rebucketized. While Lucia acknowledged that the slideshow made no explicit disclosure that the backtests did not rebucketize, he testified that seminar attendees would nonetheless have known that the backtests were not rebucketized because he explained to them that rebalancing is not always necessary. Lucia testified that, during the seminars, he drew out a bucket strategy by hand to show that the stock bucket does not have to be rebalanced and mentioned an academic article by Sandeep Singh, Ph.D., CFA, and John Spitzer, Ph.D., finding that retirees "could live off of the dividends and the income stream from the equity portfolio and an annuity contract" without rebalancing.

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[49] Plum similarly testified that "[p]utting a hundred percent into stocks" is "not a Buckets of Money strategy," and that RJLC did not believe investors "should be a hundred percent in stock."

[50] Lucia also wrote in a letter to RJLC clients dated October 9, 2008, that he "would never – NEVER – advocate being 100% invested in stocks."

No evidence corroborates Lucia's testimony on this point. To the contrary, the Webinar shows that Lucia diagramed the bucket strategy and mentioned the Singh/Spitzer article to criticize the "rebalancing method," which involves withdrawing income from a retirement portfolio on a pro rata basis and rebalancing the entire portfolio annually. Lucia stated in the Webinar that the Singh/Spitzer article found that the "rebalancing method" is inferior to the BOM strategy. Lucia did not state in the Webinar that rebalancing was unnecessary in following the BOM strategy after Buckets #1 and #2 had been depleted.

E. Investor testimony

Two RJLC clients who had attended Respondents' seminars, Richard R. DeSipio and Dennis Wayne Chisholm, testified at the hearing.[51] DeSipio testified that, for the period of market stagnation starting in 1966, he understood that the BOM strategy was "backtested or checked out and that it held up relatively well compared to the other three investment programs," and that the 1966 backtest used "actual performance data" and "average inflation" that accurately reflected inflation during that historical era. DeSipio testified that he thought the 1966 backtest showed "that over a longer projected period of time, certainly for '66 going forward, that [the BOM strategy] held up under the various market conditions that occurred over the years."

DeSipio testified that if he knew the inflation rate used in the 1966 backtest was not the historical rate

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[51] DeSipio attended a seminar in Philadelphia, Pennsylvania in 2007, and Chisholm attended a seminar in Portland, Oregon in 2007.

he would have "come to question" the backtest's results, and that it would have been an important factor for him to know that the model BOM portfolio would have been reduced to $0 in twenty years if Respondents had used historical inflation rates and deducted advisory fees in the backtest. DeSipio also testified that he does not recall Lucia disclosing that the 1966 backtest did not rebucketize the model BOM portfolio. DeSipio testified that he would not want his entire retirement portfolio to be invested in stocks, as was done here in backtesting the BOM strategy without rebucketizing.

Chisholm testified that he understood from the seminar that a bear market "would not be an issue" for the model BOM portfolio "because [the strategy] was a proven method of investing, that it had been backtested," and "would do well over good times as well as bad times." Chisholm testified that in deciding whether to become an RJLC client, it would have been important to him to know that the model BOM portfolio would have been exhausted in sixteen years if the 1973 backtest had used historical inflation. Chisholm testified that "it would have lessened his confidence in" the backtests if he had known that 3% inflation was not the historical rate.

Chisholm testified that Lucia did not say anything at the seminar about the availability of REITs in 1966 and that he would have wanted to know if REITs were not readily available in evaluating the value of the 1966 backtest. Chisholm testified that Lucia emphasized during the seminar that portfolio assets be rebucketized but did not disclose that the 1966 and 1973 backtests did not rebucketize. Chisholm testified that he assumed that the backtests rebucketized and that he would have liked to have known that they did not

rebucketize. Like DeSipio, Chisholm testified that he would not want his entire retirement portfolio invested in stocks.

III. Discussion

A. RJLC willfully violated Advisers Act Sections 206(1), (2), and (4).

1. Legal Standard

Advisers Act Sections 206(1), (2), and (4) make it unlawful for an investment adviser, by jurisdictional means,[52] "directly or indirectly: (1) to employ an device scheme or artifice to defraud any client or prospective client; (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client; . . . or (4) to engage in any act, practice, or course of business which is fraudulent, deceptive, or manipulative."[53] There is significant overlap among Sections 206(1),

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[52] Respondents do not dispute that RJLC was an investment adviser or that the Commission has jurisdiction by virtue of their actions in interstate commerce. Respondents also do not dispute that they acted willfully, which is shown where a person intends to commit an act that constitutes a violation; it does not require that the actor "also be aware that he is violating one of the Rules or Acts." *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (internal quotation marks and citation omitted).

[53] 15 U.S.C. § 80b-6(1), (2), & (4). Section 206(4) further provides that "[t]he Commission shall, for the purposes of this paragraph (4) by rules and regulations define . . . such acts, practices, and courses of business as are fraudulent, deceptive, or manipulative." *Id.* § 80b-6(4). But to violate Section 206(4), there is no precondition that one of its underlying rules, such as Rule 206(4)-1, have been violated. *See Warwick Capital Mgmt., Inc.*, Advisers Act Release No. 2694, 2008 WL 149127, at *8-9 (Jan. 16, 2008) (finding a violation of Section 206(4) without an associated rule violation).

(2), and (4),[54] the boundaries of which do not need to be delineated here. For purposes of this proceeding, it is sufficient to note that all three sections encompass the making of fraudulent misstatements of material fact and omissions of material fact necessary to make statements made not misleading.[55]

Scienter, which can be established through recklessness, is necessary to violate Section 206(1).[56] Negligence is sufficient to violate Sections 206(2) and (4).[57] Lucia's conduct and his scienter or negligence are imputed to RJLC.[58]

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[54] *Cf. John P. Flannery*, Advisers Act Release No. 3981, 2014 WL 7145625, at *14 (Dec. 15, 2014) (finding the subsections of Exchange Act Rule 10b-5 "to overlap," with each encompassing, among other things, making fraudulent misstatements of material fact), *appeal docketed*, No. 15-1080 (1st Cir. Jan. 16, 2015); *see also SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963) ("Congress intended the Investment Advisers Act of 1940 to be construed like other securities legislation enacted for the purpose of avoiding frauds, not technically and restrictively, but flexibly to effectuate its remedial purposes." (internal quotation omitted)).

[55] *Warwick Capital Mgmt.*, 2008 WL 149127, at *8-9 (finding that an investment adviser violated Sections 206(1), (2), and (4) by making false and misleading statements about its assets and performance).

[56] *Vernazza v. SEC*, 327 F.3d 851, 860 (9th Cir. 2003); *SEC v. Steadman*, 967 F.2d 636, 641 (D.C. Cir. 1992).

[57] *Steadman*, 967 F.2d at 643 n.5, 647.

[58] *A.J. White & Co. v. SEC*, 556 F.2d 619, 624 (1st Cir. 1977) (holding that a firm "can act only through its agents, and is accountable for the actions of its responsible officers"); *Warwick Capital Mgmt.*, 2008 WL 149127, at *9 n.33 ("A company's scienter is imputed from that of the individuals controlling it.").

2. Respondents made fraudulent statements and omissions in the backtest slides.

Respondents' backtest slides were misleading because: (1) they falsely stated that Respondents had backtested a model BOM portfolio; (2) they stated that backtesting proved that such a portfolio would have withstood two difficult historical market periods when actual backtesting would have shown the opposite; and (3) even using Respondents' flawed assumptions, they overstated the 1973 backtest result by over $1 million.

First, Respondents conveyed to prospective clients that they had performed actual backtests of a model portfolio following the BOM strategy. In addition to using the word "backtest" to describe their analysis, Respondents' slideshow introduced the 1966 backtest by asking, "What would have happened if you retired in 1966[?]," and introduced the 1973 backtest by asking, "Can Buckets Stand Up To The Test Of The '73/'74 Grizzly Bear?" Because of such statements, the two seminar attendees who testified at the hearing, DeSipio and Chisholm, justifiably believed that Respondents had performed backtests.

But Respondents had not actually performed backtests. The parties' experts agreed that backtests use historical data. And instead of using historical data, Respondents' backtests used assumed inflation and REIT rates. Also, it was blatantly untrue for Respondents to claim that their backtests followed the BOM strategy when they did not rebucketize the model portfolio and instead left all of its assets in stocks after safer assets had been drained for income.

The BOM strategy included rebucketization and forbade investing all portfolio assets in stocks.[59]

Second, the purported results of Respondents' backtests were misleading. Had Respondents performed actual backtests beginning in 1966 and 1973 by using historical inflation and REIT rates and rebucketizing, their model portfolio would have been shown to have exhausted its assets rather than having grown in value to $4.7 million and $1,544,789, respectively, by the end of the backtest periods.

In particular, Respondents' use of a flat 3% inflation rate made the backtest results misleading because historical inflation as measured by CPI-U was substantially higher during the backtest periods. Because annual CPI-U reached double digits in the late 1970s and early 1980s, inflation adjusted annual income would have substantially increased early in the backtest periods, thereby substantially decreasing principal and ultimately causing the model portfolio to be exhausted before the backtests ended. As discussed above, this result would not change for the 1966 backtest even using Hekman's downward adjustment to CPI-U based on the Boskin Commission corrections.[60]

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[59] As noted above, the ALJ also found that Respondents' statements about the backtests were misleading because Respondents did not inform prospective clients that the backtests did not deduct advisory fees. Given our other findings, which amply support liability and the sanctions imposed, we have determined not to reach this additional basis for liability.

[60] Hekman recalculated only the 1966 backtest using the Boskin Commission corrections; he did not also recalculate the 1973 backtest. In addition, Respondents' contention, supported by Hekman's conclusion, that CPI-U should be further reduced

In addition, Respondents' use of a flat 7% REIT dividend rate on a constant $200,000 REIT principal made the backtest results misleading because it was higher than historical REIT rates of return. As Grenadier demonstrated without contradiction, substituting data from the NAREIT All REIT Index back through 1972 resulted in REIT principal dropping to $85,646 in Respondents' 1966 backtest spreadsheet and $134,031 in Respondents' 1973 backtest spreadsheet, and lower valued portfolios as a consequence.[61] The 1966 backtest was further inflated by Respondents' use of entirely fictitious REIT rates for 1966 to 1971, a period when REITs were generally unavailable to investors.

Also, Respondents' failure to rebucketize the backtests inflated their results because, during the period when the model BOM portfolio was fully invested in stocks, S&P 500 returns were substantially higher than T-bill returns and about equivalent to publicly traded REIT returns. A rebucketized model BOM portfolio would have been invested in all three assets, not just stocks.[62]

Third, Respondents overstated the 1973 backtest result by over $1 million even using their assumptions. Respondents concede that they have no documentary support for the $1,544,789 result they presented to seminar attendees, and their expert, using

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to account for reduced retiree spending is not persuasive because, as Grenadier observed, it unjustifiably conflates spending levels with inflation.

[61] Respondents did not demonstrate that Grenadier's calculations would be materially different using the NAREIT Equity Index instead of the NAREIT All REIT Index.

[62] Lucia also admitted in testimony that not rebucketizing caused the backtests to show higher portfolio returns.

assumptions similar to those Respondents claim to have used, concluded that the model BOM portfolio would have been worth only $507,194 at the end of the 1973 backtest. Thus, Respondents either fabricated the 1973 backtest result or presented it to seminar attendees without ensuring its accuracy.

3. Respondents' fraudulent statements and omissions were material.

For a misleading statement to be material, "there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[63] It would have been significant to a reasonable investor in considering whether to become an RJLC client or implement the BOM strategy to know that: (i) Respondents' purported backtests did not use historical inflation or REIT rates or even follow the BOM strategy by rebucketizing; (ii) actual backtests beginning in 1966 and 1973 would have shown the model portfolio to have been exhausted by the 1980s rather than providing decades of payouts with an increase in residual principal; and (iii) Respondents presented a result for the 1973 backtest that was over $1 million higher than even their flawed assumptions would have shown.

Our conclusion is supported by testimony from prospective clients who attended Respondents' seminars. DeSipio and Chisholm testified that they would have found it important to know that Respondents' backtests did not use historical inflation and that actual backtests using historical data would have shown the model portfolio to have exhausted its assets.

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[63] *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988).

Chisholm also testified that he would have wanted to know that the backtests did not rebucketize and that REITs were not readily available in 1966. And DeSipio testified that that he would not want his entire portfolio to be invested in stocks, as was done here by not rebucketizing the backtests.

4. Respondents made the fraudulent misstatements and omissions with scienter.

Respondents acted at least recklessly.[64] Lucia designed the backtests and was responsible for the backtest slides. In approving and using the backtest slides, it was Lucia's decision to tell seminar attendees that he had backtested the BOM strategy to show how a portfolio implementing it in the past would have performed over historical time periods with specific negative market performance. But Lucia knew that the backtests were not based on historical data and did not rebucketize, and therefore knew or must have known of the risk of misleading prospective clients to believe that Respondents had performed actual backtests of a model BOM portfolio. Indeed, because Lucia admitted that the BOM strategy does not advocate keeping all portfolio assets in stocks, he knew or must have known that it was untrue to claim that the backtests followed the BOM strategy.

Also, Lucia knew or must have known that the backtest results he presented were misleading. Lucia

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[64] The recklessness required to violate Section 206(1) "is not merely a heightened form of ordinary negligence; it is an 'extreme departure from the standards of ordinary care, . . . which presents a danger of misleading buyers or sellers that is either known to the [respondent] or is so obvious that the actor must have been aware of it.'" *Steadman*, 967 F.2d at 641-2 (quoting *Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977)).

knew that: (i) actual inflation was higher than 3% early in the backtests and fluctuated annually; (ii) REITs did not produce flat 7% dividend rates on flat principal; and (iii) not rebucketizing caused the backtests to show higher portfolio returns.

Finally, Lucia acted recklessly, at the very least, in presenting the 1973 backtest results without ensuring their accuracy. As discussed above, Respondents provided no support for their 1973 backtest and Hekman was unable to replicate its results. Lucia also admitted in testimony that the 1973 backtest slides misstated the methodology Respondents purportedly used for the backtest.

B. Lucia willfully aided and abetted and caused RJLC's violations of Advisers Act Sections 206(1), 206(2), and 206(4).

To establish aiding and abetting liability, the Commission must find: (i) a primary violation of the securities laws by RJLC; (ii) that Lucia substantially assisted RJLC's primary violation; and (iii) that Lucia provided such assistance with the requisite scienter.[65] The scienter requirement may be satisfied by evidence that Lucia knew of or recklessly disregarded the wrongdoing and his role in furthering it.[66]

Because the primary violations of Advisers Act Sections 206(1), 206(2), and 206(4) are premised on the imputation of Lucia's conduct and scienter to RJLC for the reasons discussed above, we find that Lucia satisfies the elements for aiding and abetting liability. Lucia substantially assisted RJLC's primary

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[65] *Howard v. SEC*, 376 F.3d 1136, 1143 (D.C. Cir. 2004); *Eric J. Brown*, Advisers Act Release No. 3376, 2012 WL 625874, at *11 (Feb. 27, 2012).

[66] *Brown*, 2012 WL 625874, at *11.

violations because he designed the backtests, was responsible for the backtest slides, and made the material misstatements about the backtests to seminar attendees. Lucia provided such assistance with scienter because he knew or must have known that the statements he made about the backtests to seminar attendees were misleading. Because we find that Lucia aided and abetted RJLC's primary violations, "he necessarily was a cause of the violations."[67]

C. RJLC willfully violated, and Lucia willfully aided and abetted and caused RJLC's violation of, Advisers Act Section 206(4) and Rule 206(4)-1(a)(5) thereunder.

Advisers Act Rule 206(4)-1(a)(5) provides that it constitutes a fraudulent act, practice, or course of business within the meaning of Section 206(4) for an investment adviser "directly or indirectly, to publish, circulate, or distribute any advertisement . . . which contains any untrue statement of a material fact, or which is otherwise false or misleading."[68] The Rule defines "advertisement" to include "any notice, circular, letter *or other written communication* addressed to more than one person . . . which offers . . . investment advisory service[s] with regard to securities."[69] As the Ninth Circuit found, "[t]he term 'advertisement' is broadly defined in Rule 206(4)-1(b)" and includes "[i]nvestment advisory material which promotes advisory services for the purpose of inducing potential clients to subscribe to those services."[70]

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[67] *Zion Capital Mgmt. LLC*, Advisers Act Release No. 2200, 2003 WL 22926822, at *7 (Dec. 11, 2003).

[68] 17 C.F.R. § 275.206(4)-1(a)(5).

[69] 17 C.F.R. § 275.206(4)-1(b) (emphasis added).

[70] *C.R. Richmond & Co.*, 565 F.2d at 1104.

Respondents urge us to apply the same reading of Rule 206(4)-1 as did the ALJ, who found that their slideshow presentation was not an "advertisement" because it did not qualify as a "written communication" under Rule 206(4)-1(b).[71] The ALJ based his finding on precedent that he understood to hold that a "written communication" includes "only traditional media, including books, newsletters, and newspaper and magazine advertisements."[72] And because "[t]here is no evidence that slideshow printouts or synopses thereof were handed out to seminar participants or otherwise published in printed or handwritten form at the seminars," the ALJ found that the slideshow presentation was not a "'written communication' as that term has been interpreted."[73]

But none of the cases cited by the ALJ, nor any other case, has held that only traditional media qualifies as a "written communication" under Rule 206(4)-1(b). To the contrary, the cases cited by the ALJ merely found that a "written communication" *includes* newsletters, newspaper advertisements, and books.[74] They did not exclusively define those words.

The plain language of Rule 206(4)-1(b) also does not limit a "written communication" to traditional media or require that a "written communication" be in

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[71] *Raymond J. Lucia Cos.*, 2013 WL 6384274, at *50-51.

[72] *Id.* at *51. The ALJ cited the following cases as precedent: *SEC v. Suter*, No. 81-3865, 1983 WL 1287, at *11-12 (N.D. Ill. Feb. 11, 1983), *aff'd*, 732 F.2d 1294 (7th Cir. 1984); *SEC v. Lindsey-Holman Co.*, No. 78-54-MAC, 1978 WL 1129, at *2-3 (M.D. Ga. Aug. 6, 1978); *C.R. Richmond & Co.*, 565 F.2d at 1104.

[73] *Raymond J. Lucia Cos.*, 2013 WL 6384274, at *51.

[74] *Suter*, 1983 WL 1287, at *11-12; *Lindsey-Holman Co.*, 1978 WL 1129, at *2-3; *C.R. Richmond & Co.*, 565 F.2d at 1104.

hard-copy rather than electronic or projected form.[75] The Rule's only limitations on what qualifies as a "written communication" are that it be "written"[76] and a "communication."[77] Both of those limitations are met here. There is no question that the slideshow was written. And its projection onto a screen along with Lucia's presentation of its contents was a communication to seminar attendees. Thus, the slideshow was a "written communication" within the meaning of Rule 206(4)-1(b).

The slideshow also meets the two additional requirements of the Rule's broad definition of "advertisement." First, the slideshow was addressed to more than one person—typically to an audience of one hun-

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[75] Although not specifically interpreting the phrase, "written communication," we have previously advised that, under Rule 206(4)-1, "electronically disseminated advertisements are subject to the same prohibitions against misleading disclosure as advertisements in paper." *Use of Electronic Media by Broker-Dealers, Transfer Agents, and Investment Advisers*, Advisers Act Release No. 1562, 1996 WL 242059, at *6 (May 9, 1996); *see also id.* at *2 n.4 ("[T]he antifraud provisions of . . . section 206 of the Advisers Act and the rules thereunder, apply to information delivered and communications transmitted electronically, to the same extent as they apply to information delivered in paper form.").

[76] At the time we adopted Rule 206(4)-1 in 1961, Webster's Third New International Dictionary defined "written" as the past participle of "write," which it in turn defined as, *inter alia*, (i) "to set forth in written language . . . reveal, describe, treat of, or depict by means of words"; and (ii) "to form or produce letters, words, or sentences with a pen, pencil, or machine." Webster's Third New Int'l Dictionary 2640-41 (1961).

[77] Webster's Third New International Dictionary defined "communication" as, *inter alia*, (i) "the act or action of imparting or transmitting"; (ii) "facts or information communicated"; and (iii) "interchange of thoughts or opinions." *Id.* at 460.

dred to five hundred people. Second, the slideshow offered RJLC's investment advisory services with regard to securities. Indeed, Respondents used the slideshow presentation to generate leads for RJLC. To that end, Respondents handed out response cards for seminar attendees to complete if they wanted to meet with an RJLC advisor. Lucia also repeatedly offered RJLC's services throughout the Webinar presentation of the slideshow. And Respondents treated the slideshow as marketing and advertising material requiring review by RJLC's broker-dealers.

The remaining elements of Rule 206(4)-1 have also been satisfied. By projecting the slideshow onto a screen and presenting its contents during the seminars, Lucia published, circulated, and distributed it.[78] And as set forth above, the slideshow contained untrue statements of material fact and was misleading.

Accordingly, we find that RJLC willfully violated Section 206(4) on the additional ground that its conduct constitutes a fraudulent act, practice, or course of business as defined in Rule 206(4)-1(a)(5). And because that primary violation is premised on the imputation of Lucia's conduct and scienter to RJLC as discussed above, we find that Lucia willfully aided and abetted and caused RJLC's violation of Section 206(4) and Rule 206(4)-1(a)(5).

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[78] Webster's Third New International Dictionary defined "publish" as, *inter alia*: (i) "to declare publicly"; (ii) "to impart or acknowledge to one or more persons"; and (iii) "to place before the public (as through a mass medium)." Webster's at 1837. It defined "circulate" as, *inter alia*, (i) "to spread widely"; and (ii) "to cause to pass from person to person and [usually] to become widely known." *Id.* at 409. And it defined "distribute" as, *inter alia*, "to give out or deliver esp. to the members of a group." *Id.* at 660.

D. Respondents' arguments against liability lack merit.

1. Respondents contend that they did not mislead prospective clients.

Respondents claim that they explicitly told seminar attendees, through both the slides and the actual words spoken by Lucia, that they were presenting hypothetical illustrations using hypothetical assumptions. Respondents claim that the slides themselves "specifically and repeatedly explained that '[r]ates of return are hypothetical in nature and are for illustrative purposes only'" and that "[t]his is a hypothetical illustration and is not representative of an actual investment." And Respondents claim that Lucia, in presenting the slides, "expressly informed seminar attendees that he was using *hypothetical, pretend, assumed* rates of return."[79]

We find that such statements did not change the overall impression that Respondents had performed backtests showing how the BOM strategy would have

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[79] Respondents also contend that seminar attendees would have understood that the inflation and REIT rates used were hypothetical because: (i) the attendees were "comprised primarily of retirees and near-retirees who had lived through periods of high inflation, [and no reasonable attendee] would have understood the 3% annual inflation rate . . . to be based on actual historical inflation"; and (ii) "a reasonable investor understands that in reality return rates fluctuate, and respondents' illustrations, rather than being based on real-life data, incorporated an assumed constant rate of return." But DeSipio and Chisholm did not make such assumptions. To the contrary, they justifiably understood from Respondents' presentation that Respondents had used historical rates in their backtests.

performed during the two historical periods.[80] In addition to using the word "backtest," Respondents' slideshow introduced the 1966 backtest by asking, "What would have happened if you retired in 1966[?]," and introduced the 1973 backtest by asking, "Can Buckets Stand Up To The Test Of The '73/'74 Grizzly Bear?" And the two seminar attendees who testified understood from Lucia's presentation that Respondents had performed backtests showing that the BOM strategy could increase a portfolio's value during the two historical periods.[81]

Moreover, regardless of Respondents' disclaimers about hypothetical rates, Respondents misled seminar attendees by not rebucketizing the 1966 and 1973 backtests. In other words, it would have been just as misleading for Respondents not to rebucketize if they

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[80] *Cf. C.R. Richmond & Co.*, 565 F.2d at 1106-07 (finding that advertisements were "deceptive and misleading in their overall effect," in violation of Advisers Act Section 206(4) and Rule 206(4)-1, "even though [it might be argued that] when narrowly and literally read, no single statement of a material fact was false" (quoting *Spear & Staff, Inc.*, Advisers Act Release No. 188, 1965 WL 88746, at *3 (1965))); *see also id.* at 1105 ("[C]onduct with respect to [Rule 206(4)-1] is to be measured from the viewpoint of a person unskilled and unsophisticated in investment matters, . . . and the terms 'fraud' and 'deceit' are used in a flexible and non-technical sense to effectuate the [Advisers] Act's remedial purposes.").

[81] Respondents also contend that Lucia referenced "direct ownership in real estate" when discussing the period from 1966 to 1971 in the backtest. But the 1966 backtest slides specifically stated that "*REIT* returns are based on a 7% annual return," and the 1966 backtest spreadsheet referred only to REITs. And Respondents did not clarify during the seminars that REITs were generally unavailable from 1966 to 1971 and that they actually meant "direct ownership in real estate" when discussing that period.

had in fact stated that they were presenting a hypothetical illustration that purportedly followed the BOM strategy as it was for them not to rebucketize what was described as a backtest. Rebucketizing was a key aspect of the BOM strategy, and keeping all assets in stocks—the result of not rebucketizing—contravened the strategy (and substantially inflated the resulting returns). Thus, not rebucketizing made it untrue for Respondents to claim that their model portfolio, whether presented as a "hypothetical illustration" or a backtest, followed the BOM strategy.

Respondents' 1973 backtest results were also false regardless of disclaimers about hypothetical rates. As noted, Respondents' expert did not come within $1 million of the 1973 backtest results using Respondents' own hypothetical inflation rate and other assumptions similar to those that Respondents claim to have used. Consequently, even if Respondents were presenting hypothetical illustrations and not backtests, it was misleading for them to present such grossly inaccurate results.

Respondents contend that the only purpose of the seminar presentation was to compare BOM to three other strategies, and that the Division failed to show that, had Respondents "used historical data rather than hypothetical assumptions . . . [the BOM] strategy would have failed to outperform the other investment strategies illustrated."[82] For example, Respondents assert that they used the same 3% inflation rate for

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[82] Respondents similarly argue that there can be no finding of materiality here because the Division has made no "allegation (much less an evidentiary showing) . . . that, had Mr. Lucia used actual rates of return . . . and 'rebucketized,' his recommended strategy would not have outperformed the alternative approaches illustrated in the seminar."

each of the strategies illustrated and there was no showing that, "under a higher inflation rate, Lucia's strategy would not have nonetheless outperformed the alternatives he illustrated."

We reject this argument because the purpose of the backtest slides was not only to compare strategies but also to show the efficacy of the BOM strategy during difficult historical market periods. Respondents misled seminar attendees to believe that, as Chisholm testified, BOM "was a proven method of investing, that it had been backtested," and "would do well over good times as well as bad times." But actual backtests would have shown that the BOM strategy would not have done well over the two historical "bad times" chosen. And again, regardless of this contention, not rebucketizing the backtests and presenting grossly inaccurate 1973 backtest results made Respondents' representations false and misleading.

Respondents also assert four reasons why their assumptions were reasonable and not used to mislead seminar attendees. First, Respondents contend that they submitted "expert testimony supporting the reasonableness of the assumed inflation rates and REIT return rates used in the illustrations." For example, Hekman "testified that the use of a 3% inflation rate for hypothetical retirement planning calculations is universally recognized," and Gannon "testified that a 7% REIT return rate for 1966-2003 . . . was reasonable and supported by available indices." We reject this argument because Hekman and Gannon made clear that their opinions about the reasonableness of Respondents' inflation and REIT rates did not apply to backtests but rather to hypothetical illustrations, and Respondents led seminar attendees to believe that they had performed backtests.

Second, Respondents contend that it was reasonable not to rebucketize the backtests because to do so "would have been highly speculative" and potentially led to accusations of manipulating rebalancing dates because the "strategy illustrated . . . did not represent an actual portfolio with specific investments, but rather a general approach to diversification," and "[d]eciding when and how to shift asset classes would turn entirely on a client's individualized holdings and the market conditions at the time." We reject this contention because, even if Respondents genuinely held these concerns, it was misleading for them not to disclose to seminar attendees that that the backtest results were inflated because they did not rebucketize. Respondents' contention also seems insincere considering that Respondents had no apparent difficulty or reservation in shifting asset classes in the backtest spreadsheets from REITs to T-bills.

Third, Respondents contend that their assumptions were reasonable because there is no established definition of "backtest" precluding the use of assumed rates. Respondents contend that to base liability here on "a firm definition not found in the securities laws," would violate due process by denying Respondents "fair notice of what conduct is required or proscribed," and be an abuse of discretion by imposing "regulatory changes through litigation" rather than rulemaking. Respondents also contend that "[e]ven if one were to posit that Mr. Lucia misused the term 'backtest,' it cannot be denied that he informed visitors of his seminars exactly how he was using it."

We reject these arguments. In finding liability, we need not define "backtest" in all contexts, we just need to assess its use by Respondents here. That use was in conjunction with other statements that misled

seminar attendees to believe that Respondents had analyzed how a model portfolio would have performed had it implemented the BOM strategy in the past. Respondents never informed attendees that their assumptions would not actually show, as they claimed, whether the model BOM portfolio could "stand up to" the market challenges starting in 1966 or 1973.[83]

Fourth, Respondents contend that their assumptions were reasonable because it was industry practice to use assumed rates in backtests. As an example of that practice, Respondents point to the American Funds brochure "that included multiple illustrations of 'back-testing withdrawal rates,' all using hypothetical (rather than actual) inflation rates over an historical period." But Respondents introduced no expert testimony to establish industry practice, and their own inflation and REIT experts agreed that backtests use historical rates. And while the backtests in the American Funds brochure used an assumed 4% inflation rate, two other brochures in the record, from Fidelity and Financial Engines Income+, reported the results of backtests that appear to have used historical stock, bond, and inflation rates.

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[83] Respondents similarly contend that we would violate due process if we interpreted "written communication" in Rule 206(4)-1 to include their live slideshow presentation, and that "the appropriate way to bring [the rule] up to date is through rulemaking." We also reject this argument because, as discussed above, Rule 206(4)-1 has discernible parameters that gave Respondents fair notice that their conduct fell within its scope. And even if we were applying a new interpretation of the rule, "[i]t is well settled that an agency 'is not precluded from announcing new principles in an adjudicative proceeding. . . .'" *Cassell v. FCC*, 154 F.3d 478, 486 (D.C. Cir. 1998) (quoting *NLRB v. Bell Aerospace Co.*, 416 U.S. 267, 294 (1974)).

2. Respondents contend that their statements about the 1966 and 1973 backtests were not material.

Respondents make various other arguments that do not concern the validity of the backtests, but focus more on materiality. Respondents assert that their presentation cannot have been material because they did not recommend or sell securities at the seminars, and it is undisputed that their disclosures to attendees who eventually became Firm clients were "100% complete and accurate." But .liability under Section 206 does not require that the fraudulent conduct be in connection with the offer or sale of securities.[84] To the contrary, Section 206 includes within its scope misrepresentations that are not specific to a client investment decision.[85]

Respondents also contend that they "submitted unrebutted evidence at the hearing showing that after [they] ceased using the illustrations in question once

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[84] *SEC v. Lauer*, No. 03-80612-CIV, 2008 WL 4372896, at *24 (S.D. Fla. Sept. 24, 2008), *aff'd*, 478 F. App'x 550 (11th Cir. 2012); *see also Applicability of the Investment Advisers Act*, Advisers Act Release No. 1092, 1987 WL 112702, at *9 (Oct. 8, 1987) (staff interpretive release stating that the Section 206 provisions "do not refer to dealings in securities but are stated in terms of the effect or potential effect of prohibited conduct on the client").

[85] *See, e.g., SEC v. C.R. Richmond & Co.*, 565 F.2d 1101, 1106 (9th Cir. 1977) (investment adviser violated Section 206 by making misrepresentations in a book and newsletter concerning its investment strategy and the results of a model portfolio); *see also Applicability of the Investment Advisers Act*, 1987 WL 112702, at *9 (staff interpretive release stating that "the Commission has applied Sections 206(1) and (2) in circumstances in which the fraudulent conduct arose out of the investment advisory relationship between an investment adviser and its clients, even though the conduct does not involve a securities transaction").

concerns were raised by the SEC examination staff [in 2010], the response rate of seminar attendees who filled out contact cards requesting to meet with an RJLC adviser did not decline." We find that the response cards are not determinative of materiality because they do not show whether attendees would have expressed interest in the Firm if they had been told that backtests showed the model BOM portfolio exhausting its assets during the two historical periods. This is because Respondents never told the truth about the backtests; they simply stopped using the backtest slides. And even if the response cards were relevant to materiality, Respondents introduced insufficient evidence to establish what the cards showed. Respondents' contention is based solely on vague testimony from Lucia's son that during the periods before and after Respondents stopped using the backtest slides, "basically the same" percentage of seminar attendees who filled out response cards checked a box to meet with a financial advisor.[86]

3. Respondents contend that they cannot have acted with scienter.

Respondents make various arguments that Lucia cannot have acted with scienter, and that he was, at worst, negligent in that his "hypothetical illustrations . . . were inartfully prepared." Respondents contend that Lucia "testified that he subjectively believed his use of the term 'backtest' encompassed the utilization

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[86] Lucia's son testified that based on response card data, from January to June 2010, a period when the slides were used, about 50% of seminar attendees wanted to meet with a financial advisor, and from January to June 2011, when the slides were no longer used, about 47% of seminar attendees wanted to meet with a financial advisor.

of hypothetical information." We reject this self-serving contention because it is contradicted by Lucia's representations to seminar attendees that the backtest slides showed how a portfolio implementing the BOM strategy in 1966 or 1973 would have performed. In other words, our finding of liability does not hinge on Lucia's use of the word "backtest." Lucia made numerous other statements suggesting that the slides reflected historical results, and he knew or must have known that using hypothetical data in the backtests would not reflect historical results.

Respondents also deny any scienter by pointing to "third party review [of the backtest slides] by both the registered broker-dealers who had supervisory oversight" of the Firm,[87] as well as Commission staff in a 2003 examination of the Firm,[88] who never told Respondents "that the slides were in any way misleading." Respondents contend that they therefore were "not aware of red flags suggesting that the slides were misleading." We reject these arguments. First, Respondents were well aware of the facts that rendered the backtest slides misleading for the reasons discussed above, and thus any reliance they placed on third party review would not have been reasonable.[89] Second, there is no evidence that: (i) Respondents

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[87] Respondents' registered broker-dealers, Securities America (from 2002 to 2007) and First Allied (from 2007 to 2011), reviewed RJLC's marketing and advertising material, including the slideshow, before it was distributed publicly.

[88] The examination was conducted by the Division of Investment Management's compliance office, a precursor office to the Commission's Office of Compliance Inspections and Examinations ("OCIE").

[89] *Cf. Flannery*, 2014 WL 7145625, at *33 (rejecting reliance-on-counsel defense, in part, because respondent "was well aware of the facts that rendered the statements at issue misleading").

brought the backtests to the attention of the Commission staff or broker-dealers; (ii) Respondents provided any support for the backtest slides that would have permitted a meaningful review of their content; or (iii) the Commission staff or broker-dealers addressed the backtests with Respondents. Thus, we are not presented with a situation where a third party told Respondents that the backtest slides were not misleading and Respondents relied on that advice. To the contrary, the Commission staff told Respondents in a deficiency letter dated December 12, 2003, that RJLC "should not assume that [its] activities not discussed in this letter are in full compliance with the federal securities laws."

As support for this last contention, Respondents point to *SEC v. Slocum, Gordon, & Co.*, in which the court concluded that the defendant investment adviser could not be found to have intentionally omitted material facts about its account structure (which created a potential conflict of interest by commingling firm and client funds) from its Form ADV in violation of Advisers Act Section 207 and Rule 204-1(c).[90] The court found that it was reasonable for the defendant to believe that its account structure complied with the securities laws because two Commission examinations and annual independent auditor examinations failed to identify issues with it.[91] But *Slocum* is inapposite because the defendant relied on the advice of counsel in structuring its accounts and subsequently brought its account structure to the Commission's attention.[92] Here, there is no evidence that Respondents relied on counsel or brought the backtest slides to the

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[90] 334 F. Supp. 2d 144 (D.R.I. 2004).

[91] *Id.* at 180-82.

[92] *Id.* at 160-61.

Commission's attention.

E. Respondents' Appointments Clause argument lacks merit.

Respondents argue that the ALJ who presided over this matter and issued the initial decision, ALJ Cameron Elliot, was not appointed in a manner consistent with the Appointments Clause of the Constitution.[93] Respondents further claim that, in light of this purported constitutional violation, the proceedings "are themselves invalid and any resulting orders should be vacated." We find that the appointment of Commission ALJs is not subject to the requirements of the Appointments Clause.[94]

Under the Appointments Clause, certain high-

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[93] Congress has empowered "[e]ach agency [to] appoint as many administrative law judges as are necessary," and it has established a comprehensive scheme to govern the details of ALJs' employment in the civil service. 5 U.S.C. §§ 3105, 1101 *et seq.*; *see also* 15 U.S.C. § 78d-1(a) (authorizing the Commission to delegate functions to "an administrative law judge"); Exchange Act Section 4(b), 48 Stat. 885 (original Exchange Act provision authorizing the Commission to appoint "examiners"). The Commission has for many decades relied upon ALJs to prepare initial decisions in its administrative proceedings.

[94] The constitutional claims raised here implicate many "threshold questions" regarding the Commission's rules and practices. *Elgin v. Dep't of Treasury*, 132 S. Ct. 2126, 2140 (2012); *see also Thunder Basin Coal Co. v. Reich*, 510 U.S. 200, 214-15 (1994). In the course of considering the constitutional claims, we address those questions and legal principles. It is important that the Commission have an opportunity to address constitutional issues in the first instance, as it has in the past. *See, e.g.*, *Gary M. Kornman*, Exchange Act Release No. 59403, 2009 WL 367635, at *12 (Feb. 13, 2009) (Double Jeopardy claim); *Vladen Vindman*, Securities Act Release No. 8670, 2006 WL 985308, at *11 & n.60 (Apr. 14, 2006) (Seventh Amendment claim).

level government officials must be appointed in particular ways: "Principal officers" must be appointed by the President (and confirmed by the Senate), while "inferior officers" must be appointed either by the President, the heads of departments, or the courts of law.[95] The great majority of government personnel are neither principal nor inferior officers, but rather "mere employees" whose appointments are not restricted by the Appointments Clause.[96] It is undisputed that ALJ Elliot was not appointed by the President, the head of a department, or a court of law.[97] Respondents therefore contend that his appointment violates the Appointments Clause because, in their view, he should be deemed an inferior officer. The Division counters that he is an employee and thus there was no violation of the Appointments Clause.

Our consideration of this question is guided by the D.C. Circuit's decision in *Landry v. FDIC*, which addressed whether ALJs should be deemed inferior officers or employees.[98] *Landry* held that, for purposes of the Appointments Clause, ALJs at the Federal De-

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[95] The Clause provides that the President "by and with the advice and consent of the Senate, shall appoint . . . officers of the United States . . . but the Congress may by law vest the appointment of such inferior officers, as they think proper, in the President alone, in the courts of law, or in the heads of departments." U.S. Const. art. II, §2, cl. 2.

[96] *Landry v. FDIC*, 204 F.3d 1125, 1134 (D.C. Cir. 2000) (quoting *Freytag v. Commissioner*, 501 U.S. 868, 882 (1991)); *Buckley v. Valeo*, 424 U.S. 1, 126 (1976).

[97] The Commission constitutes the "head of a department" for purposes of the Appointments Clause when its commissioners act collectively. *See Free Enter. Fund v. Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 512-13 (2010).

[98] *Landry*, 204 F.3d at 1130-34.

posit Insurance Corporation ("FDIC") who oversee administrative proceedings to remove bank executives are employees rather than inferior officers. *Landry* explained that the touchstone for determining whether adjudicators are inferior officers is the extent to which they have the power to issue "final decisions."[99] Although ALJs at the FDIC take testimony, conduct trial-like hearings, rule on the admissibility of evidence, have the power to enforce compliance with discovery orders, and issue subpoenas, they "can never render the decision of the FDIC."[100] Instead, they issue only "recommended decisions" which the FDIC Board of Directors reviews *de novo*, and "[f]inal decisions are issued only by the FDIC Board."[101] The ALJs thus function as aides who assist the Board in its duties, not officers who exercise significant authority independent of the Board's supervision. Because ALJs at the FDIC "have no such powers" of "final decision," the D.C. Circuit "conclude[d] that they are not inferior officers."[102]

The mix of duties and powers of the Commission's ALJs are very similar to those of the ALJs at the FDIC. Like the FDIC's ALJs, the Commission's ALJs conduct hearings, take testimony, rule on admissibility of evidence, and issue subpoenas. And like the FDIC's ALJs, the Commission's ALJs do not issue the final decisions that result from such proceedings. Just as the FDIC's ALJs issue only "recommended decisions" that are not final, the Commission's ALJs issue

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[99] *Id.* at 1133-34.

[100] *Id.* at 1133.

[101] *Id.*

[102] *Id.* at 1134.

"initial decisions" that are likewise not final.[103] Respondents may petition us for review of an ALJ's initial decision,[104] and it is our "longstanding practice [to] grant[] virtually all petitions for review."[105] Indeed, we are unaware of any cases which the Commission has not granted a timely petition for review. Absent a petition, we may also choose to review a decision on our own initiative,[106] a course we have followed on a number of occasions.[107] In either case, our rules expressly provide that "the initial decision [of an ALJ]

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[103] *See* 17 C.F.R. § 201.360(a)(1) & (d). We note that the FDIC Board has discretion to "limit the issues to be reviewed to those findings and conclusions to which opposing arguments or exceptions have been filed by the parties." 12 C.F.R. § 308.40(c)(1).

[104] 17 C.F.R. § 201.411(b).

[105] Rules of Practice, Exchange Act Release No. 35833, 1995 WL 368865, at *80-81 (June 9, 1995); *see also* Rules of Practice, Exchange Act Release No. 33163, 1993 WL 468594, at *59 (Nov. 5, 1993) (explaining that we are "unaware of any case in which the Commission has declined to grant a petition for review"). We reiterated this policy in the context of amendments to our Rules of Practice in 2004 that eliminated the filing of oppositions to petitions for review. We deemed such oppositions pointless, "given that the Commission has long had a policy of granting petitions for review, believing that there is a benefit to Commission review when a party takes exception to a decision." Proposed Amendments to the Rules of Practice and Related Provisions, Exchange Act Release No. 48832, 2003 WL 22827684, at *13 (Nov. 23, 2003).

[106] 17 C.F.R. § 201.411(c); *see also* 15 U.S.C. § 78d-1(b) (providing that "the Commission shall retain a discretionary right to review the action of any . . . administrative law judge . . . upon its own initiative or upon petition").

[107] *See, e.g.*, *Dian Min Ma*, Exchange Act Release No. 74887, 2015 WL 2088438, at *1 (May 6, 2015) ("determin[ing] to review the [ALJ's] decision on [our] own initiative," setting aside the initial decision in part, and providing that "as modified," the initial decision "has become the final decision of the Commission"); *Michael Lee Mendenhall*, Exchange Act Release No. 74532, 2015

shall not become final."[108] Even where an aggrieved person fails to file a timely petition for review of an initial decision and we do not order review on our own initiative, our rules provide that "*the Commission* will issue an order that the decision has become final," and it "becomes final" only "upon issuance of the order" by the Commission.[109] Under our rules, no initial decision becomes final simply "on the lapse of time" by operation of law; instead, it is "the Commission's issuance of a finality order" that makes any such decision effective and final.[110] Moreover, as does the FDIC, the

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WL 1247374, at *1 (Mar. 19, 2015) ("determin[ing] *sua sponte* to vacate the [ALJ's] initial decision"); *George C. Kern, Jr.*, Exchange Act Release No. 29356, 1991 WL 284804, at *1 (June 21, 1991) ("On its own initiative, the Commission ordered review of the [ALJ's] initial decision . . . .").

[108] 17 C.F.R. § 201.360(d)(1).

[109] 17 C.F.R. § 201.360(d)(2) (emphasis added). The effect of this rule, which was enacted pursuant to our general rulemaking authority under the securities laws, is that our ALJs' initial decisions (like the FDIC's ALJs' recommended decisions) do not become the final and effective decision of the agency without affirmative action on our part—specifically, our issuance of a finality order. *See, e.g.*, *Goolu, Inc.*, Exchange Act Release No. 71788, 2014 WL 1213742 (Mar. 25, 2014); *L. Rex Andersen, CPA*, Exchange Act Release No. 63209, 2010 WL 42[illegible]161 (Oct. 28, 2010); *David A. Zwick*, Exchange Act Release No. 56826, 2007 WL 4145827 (Nov. 20, 2007). It is not until the issuance of such an order that the Commission's "right to exercise such review [*i.e.*, review of an initial decision on our own initiative] is declined." *See* 15 U.S.C. § 78d-1(c). In short, under our rules, an ALJ's initial decision does not "become[] the decision of the agency without further proceedings," and any theoretical distinction between the potential legal effect of an initial decision as opposed to a recommended decision is immaterial. *Cf.* 5 U.S.C. § 557(b).

[110] Exchange Act Release No. 49412, 2004 WL 503739, *12 (Mar. 12, 2004); *see also* 17 CFR § 201.360(d)(2) (providing that the Commission's "order of finality shall state the date on which sanctions . . . take effect").

Commission reviews its ALJs' decisions *de novo*. Upon review, we "may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part," any initial decision.[111] And "any procedural errors" made by an ALJ in conducting the hearing "are cured" by our "thorough, *de novo* review of the record."[112] We may also "hear additional evidence" ourselves, and may "make any findings or conclusions that in [our] judgment are proper and on the basis of the record."[113] For this reason, although ALJs may play a significant role in helping to shape the administrative record initially, it is the Commission that ultimately controls the record for review and decides what is in the record. As we have explained before, we have "plenary authority over the course of [our] administrative proceedings and the rulings of [our] law judges—before and after the issuance of the initial decision and irrespective of whether any party has sought relief."[114]

Notwithstanding the direct relevance of *Landry*,

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[111] 17 C.F.R. § 201.411(a); *see also* 5 U.S.C. § 557(b) ("On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision . . . .").

[112] *Heath v. SEC*, 586 F.3d 122, 142 (2d Cir. 2009); *see also, e.g.*, *In the Matter of Anthony Fields*, Exchange Act Release No. 74344, 2015 WL 728005, *20 (Feb. 20, 2015) ("[O]ur de novo review cures any evidentiary error that the law judge may have made.").

[113] 17 C.F.R. §§ 201.411(a), 201.452.

[114] *Michael Lee Mendenhall*, 2015 WL 1247374, at *1. This includes authority over all evidentiary and discovery-related rulings. And the fact that our ALJs may rule on evidentiary matters and discovery issues (subject to our *de novo* review) does not distinguish them from the FDIC's ALJs in *Landry*. *See* 204 F.3d at 1134 (observing that the FDIC's ALJs make rulings on the "admissibility of evidence" and "discovery order[s]").

Respondents claim that the decision should not control here because, in their view, it "was wrongly decided." They claim that *Landry* "is inconsistent with" *Freytag v. Commissioner*, in which the Supreme Court deemed a Tax Court "special trial judge" to be an inferior officer.[115] But, as *Landry* recognized, ALJs are different from those special trial judges.[116] The far greater role and powers of the special trial judges relative to Commission ALJs, in our view, makes *Freytag* inapposite here.

First, unlike the ALJs whose decisions are reviewed *de novo*, the special trial judges made factual findings to which the Tax Court was required to defer, unless clearly erroneous.[117] *Second*, the special trial

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[115] *Freytag*, 501 U.S. at 880-82. Respondents insist that Judge Randolph's concurring opinion in *Landry* had the better reading of *Freytag*. For the reasons given in text, we reject this argument. And in any event, Respondents would not be entitled to relief even under the reasoning of the *Landry* concurrence. Our review of ALJ's decisions—like that performed by the FDIC—is *de novo*; thus, given our "*de novo* review" and our "thorough rejection of [Respondents'] various claims of error" on the merits, Respondents "suffered no prejudice" from the manner of appointment of our ALJs. *Landry*, 204 F.3d at 1144 (Randolph, J., concurring).

[116] *Landry*, 204 F.3d at 1133 (explaining that the special trial judges at issue in *Freytag* exercised "authority . . . not matched by the ALJs. . . .").

[117] *See Landry*, 204 F.3d at 1133. Respondents argue that Commission ALJs exercise significant authority because the Commission accords "considerable weight" to those ALJ credibility findings that are based on witness demeanor. *Kenneth R. Ward*, Exchange Act Release No. 47535, 2003 WL 1447865, at *10 (Mar. 19, 2003), *aff'd*, 75 F. App'x 320 (5th Cir. 2003). We do not view the fact that we accord Commission ALJs deference in the context of demeanor-based credibility determinations to afford our ALJs with the type of authority that would qualify them as inferior officers. *First*, as we have repeatedly made clear, we do not

judges were authorized by statute to "render the [final] decisions of the Tax Court" in significant, fully-litigated proceedings involving declaratory judgments and amounts in controversy below $10,000.[118] As discussed above, our ALJs issue initial decisions that are not final unless the Commission takes some further action. *Third*, the Tax Court (and by extension the court's special tax judges) exercised "a portion of the judicial power of the United States," including the "authority to punish contempts by fine or imprisonment."[119] Commission ALJs, by contrast, do not possess such authority.[120]

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accept such findings "blindly," and we will "disregard explicit determinations of credibility" when our *de novo* review of the record as a whole convinces us that a witness's testimony is credible (or not) or that the weight of the evidence warrants a different finding as to the ultimate facts at issue. *Ward*, 2003 WL 1447865, at *10; *accord Francis V. Lorenzo*, Exchange Act Release No. 74836, 2015 WL 1927763, at *10 n.32 (Apr. 29, 2015); *Ofirfan Mohammed Amanat*, Exchange Act Release No. 54708, 2006 WL 3199181, at *8 n.46 (Nov. 3, 2006); *see also Kay v. FCC*, 396 F.3d 1184, 1189 (D.C. Cir. 2005) ("The law is settled that an agency is not required to adopt the credibility determinations of an administrative law judge."). *Second*, our practice in this regard is no different from the FDIC's and so does not warrant a departure from *Landry*. *Compare [Redacted] Insured State Nonmember Bank*, FDIC-82-73a, 1984 WL 273918, at *5 (June 18, 1984) (stating, "as a general rule," that "the assessment of the credibility of witnesses" by the ALJ is given "deference" by the FDIC) *with Ramon M. Candelaria*, FDIC-95-62e, 1997 WL 211341, at *3-4 (Mar. 11, 1997) (noting that the FDIC's ALJ found respondent to be "entirely credible" but the Board rejected respondent's testimony "in light of the entire record").

[118] *Freytag*, 501 U.S. at 882.

[119] *Id.* at 891.

[120] *See* 17 C.F.R. § 201.180. The Commission's rules provide ALJs with authority to punish contemptuous conduct only in the

Based on the foregoing, we conclude that the mix of duties and powers of our ALJs is similar in all material respects to the duties and role of the FDIC's ALJs in *Landry*.[121] Accordingly, we follow *Landry*,

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following ways. If a person engages in contemptuous conduct before the ALJ during any proceeding, the ALJ may "exclude that person from such hearing or conference, or any portion thereof," or "summarily suspend that person from representing others in the proceeding in which such conduct occurred for the duration, or any portion of the proceeding." *Id.* 201.180(a). Finally, if a party fails to make a required filing or to cure a deficiency with a filing, then a Commission ALJ may enter a default, dismiss the case, decide the particular matter at issue against the person, or prohibit the introduction of evidence or exclude testimony concerning that matter." *Id.* 201.180(c). Any such decision would, of course, be subject to *de novo* Commission review. And while Commission ALJs may issue subpoenas to compel noncompliance, they are powerless to enforce their subpoenas. The Commission itself would need to seek an order from a federal district court to compel compliance. *See* 15 U.S.C. § 78u(c). In this respect, too, our ALJs are akin to the FDIC's ALJs that *Landry* found to be mere employees. *See* 12 C.F.R. §§ 308.25(h), 308.26(c), 308.34(c) (providing that an aggrieved party must apply to a federal district court for enforcement of a subpoena issued by a FDIC ALJ).

[121] Beyond *Landry*, we believe that our ALJs are properly deemed employees (rather than inferior officers) because this is how Congress has chosen to classify them, and that decision is entitled to considerable deference. *See Burnap v. United States*, 252 U.S. 512, 516 (1920). For example, Congress created and placed ALJ positions within the competitive service system, just like most other federal employees. *See infra* footnote 93. Like most other employees, an ALJ who believes that his employing agency has engaged in a prohibited personnel practice can seek redress either through the Office of Special Counsel or the Merit Systems Protection Board. *See* 5 U.S.C. §§ 1204, 1212, 1214, 1215, 1221. And ALJs—like other employees—are subject to reductions-in-force. *See id.* § 7521(b).

and we conclude that our ALJs are not "inferior officers" under the Appointments Clause.[122]

IV. Sanctions

The Division requests that we affirm the sanctions imposed below, including that (i) Lucia be barred from associating with an investment adviser, broker, or dealer; (ii) Respondents' investment adviser registrations be revoked; (iii) Respondents be ordered to cease and desist from further violations of the Advisers Act; and (iv) RJLC pay civil penalties of $250,000 and Lucia pay civil penalties of $50,000. We do so for the following reasons.

A. Bar from associating with an investment adviser, broker, or dealer

We may suspend or bar Lucia from associating with an investment adviser, broker, or dealer under Advisers Act Section 203(f) if we find that (i) he was associated with an investment adviser during the relevant period, (ii) he willfully violated, or willfully aided and abetted the violation of, the Advisers Act or

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[122] We do not find any relevance in the fact that the federal securities laws and our regulations at times refer to ALJs as "officers" or "hearing officers." There is no indication that Congress intended "officers" or "hearing officers" to be synonymous with "Officers of the United States," U.S. Const. art. II, § 2, cl. 2, and the word "officer" in our regulations has no such meaning. We also note in this regard that the Administrative Procedure Act "consistently uses the term 'officer' or the term 'officer, employee, or agent'" to "refer to [agency] staff members." Kenneth Culp Davis, *Separation of Functions in Administrative Agencies*, 61 HARV,. L. REV. 612, 615 & n.11 (1948); *see also* 1 U.S.C. § 1 ("'officer' includes any person authorized by law to perform the duties of the office"). *Cf.* 5 U.S.C. §§ 556, 557 (referring to official who presides over evidentiary hearing as the "presiding employee").

its rules, and (iii) the sanction is in the public interest.[123] In addition, if we find that the latter two elements have been established, we may also suspend or bar Lucia from associating with a broker or dealer under Section 15(b)(6) of the Securities Exchange Act of 1934.[124]

There is no question that Lucia was associated with an investment adviser, and, as discussed above, we find that he willfully aided and abetted and caused RJLC's violations of Advisers Act Sections 206(1), (2), and (4) and Rule 206(4)-1(a)(5). Thus, we must determine whether a bar is in the public interest.

In assessing whether an associational bar would be in the public interest, we consider: the egregiousness of the respondent's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the respondent's recognition of the wrongful nature of his or her conduct, the sincerity of the respondent's assurances against future violations, and the likelihood that the respondent's occupation will present opportunities for future violations.[125] The remedy is intended to "protect[] the trading public from further harm," not to punish the respondent.[126] Our inquiry is flexible, and no one factor is dispositive.[127]

Lucia's misconduct was egregious. As an invest-

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[123] 15 U.S.C. § 80b-3(f).

[124] 15 U.S.C. § 78o(b)(6)(A)(i).

[125] *See Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981).

[126] *McCarthy v. SEC*, 406 F.3d 179, 188 (2d Cir. 2005).

[127] *Kornman*, 2009 WL 367635, at *11.

ment adviser, Lucia owed fiduciary duties to his prospective clients.[128] Lucia violated those duties, and betrayed the trust and confidence of his prospective clients, by making the material misrepresentations and omissions discussed above. We have repeatedly stated that "conduct that violates the antifraud provisions of the securities laws is especially serious and subject to the severest of sanctions under the securities laws."[129]

Lucia's misconduct was recurrent: he made the material misrepresentations and omissions in the slideshow at dozens of seminars every year during the relevant period. Lucia also acted with a high degree of scienter as he knowingly or recklessly misled prospective clients for the purpose of increasing RJLC's client base and the fees generated therefrom. Thus, Lucia repeatedly and intentionally placed his and RJLC's own interests over those of his prospective clients.

Lucia has not recognized the wrongful nature of his misconduct, and his failure to do so casts doubt on his assurances against future violations. In addition, because Lucia disregarded his fiduciary duties in the past in the manner shown here there is reason to believe that he will disregard them in the future.

Lucia's various arguments do not undermine the need for a bar or argue for a lesser remedy. Lucia contends that the credibility of his assurances and his recognition of wrongdoing are demonstrated by his decision to immediately stop using the backtest slides

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[128] *Capital Gains*, 375 U.S. at 194.

[129] *Marshall E. Melton*, Advisers Act Release No. 2151, 2003 WL 21729839, at *9 (July 25, 2003); *Justin F. Ficken*, Advisers Act Release No. 2803, 2008 WL 4610345, at *3 (Oct. 17, 2008).

and withdraw his books from circulation after receiving the deficiency letter from OCIE on December 17, 2010, that outlined the deficiencies forming the basis of this proceeding.[130] These actions do weigh in Lucia's favor but they do not outweigh the concerns raised by his intentional and recurrent fraud.[131]

Lucia asserts that his occupation will not present opportunities for future violations because he has left the securities industry.[132] Lucia states that he wound

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[130] Lucia argues that his actions are comparable to those at issue in *Steadman*, in which the court vacated an injunction against an investment adviser in part because the alleged violations "were corrected immediately after the SEC notified the appellants that charges were pending." 967 F.2d at 648. But unlike our findings here, the *Steadman* court found that the defendants did not act with scienter and therefore did not violate federal securities antifraud provisions.

[131] *Cf. Kornman*, 2009 WL 367635, at *11 (stating that assurances against future misconduct "are not an absolute guarantee against misconduct in the future"; the Commission weighs them against the other *Steadman* factors in assessing the public interest.).

[132] Lucia claims that he "simply desires to continue serving as an in-demand public speaker, consultant, and media personality on retirement planning and other topics," and invites us to make clear that, if we impose a bar, such activity would not violate the bar. Lucia contends that such work is protected by the publisher exclusion to the definition of "investment adviser" in Advisers Act Section 202(a)(11), 15 U.S.C. § 80b-2(a)(11)(D), and is thus outside the scope of an associational bar. But because of "the inherent difficulty of enumerating every position that [Lucia] could take that would be prohibited by, or consistent with," a bar order, granting Lucia's request would undermine the remedial purpose of imposing a bar. *See James M. Schneider, CPA*, Exchange Act Release No. 69922, 2013 WL 3327751, at *5-6 (July 2, 2013) (order denying request that the Commission clarify that its Rule 102(e) suspension order did not preclude movant from accepting non-accounting positions). In any event, we note that

down RJLC's operations, sold its assets, and withdrew its investment adviser registration. Lucia also states that he is no longer associated with an investment adviser or broker-dealer, no longer holds a license as a registered representative, withdrew his own personal investment adviser registration, and has no intention of ever again being an investment adviser or registered representative of a broker-dealer. He also does not challenge the permanent revocation of his and RJLC's investment adviser registrations. Lucia contends that he has therefore demonstrated that his assurances against future violations are credible and that his occupation will not present opportunities for future violations.

But taking these steps does not ensure that Lucia will not seek to become associated again with an investment adviser, broker, or dealer. And like Lucia's decision to stop using the backtest slides, these steps do not make his assurances sufficient considering that he intentionally and repeatedly misled prospective clients to whom he owed fiduciary duties.[133] Thus, there is a reasonable likelihood that, without a bar, Lucia

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the publisher exclusion concerns only who is considered an investment adviser, and not whether a person is *associated with* an investment adviser. The definition for "person associated with an investment adviser" is set forth in Adviser Act Section 202(a)(17), 15 U.S.C. § 80b-2(a)(17).

[133] Also, according to FINRA's BrokerCheck, Lucia did not end his association with investment adviser RJL Wealth Management, LLC, the successor firm to RJLC, until the initial decision was first issued in July 2013, thus casting further doubt on his intention to not reenter the industry. We may take official notice of this information on BrokerCheck, available at www.finra.org/Investors/ToolsCalculators/BrokerCheck. *See* 17 C.F.R. § 201.323 (rule of practice relating to official notice).

will again threaten the public interest by reassociating with an investment adviser, broker, or dealer.

Lucia asserts that several mitigating factors justify a lesser remedy. He contends that a bar would deter businesses from working with him in his career as a public media personality and therefore "propel[] him towards personal bankruptcy." But "[f]inancial loss to a wrongdoer as a result of his wrongdoing does not mitigate the gravity of his conduct."[134]

Lucia contends that he is a "40-year industry veteran with no disciplinary record." But his lack of previous securities law violations does not outweigh the concern that, for the reasons discussed above, Lucia will pose a continuing danger to investors if a bar is not imposed. Lucia's repeated misconduct for a prolonged period demonstrates that he has a propensity for conduct that would subject the investing public to future harm.

Lucia contends that there are no allegations of misappropriation, investor losses, or complaints by any seminar attendees about the presentation. But the absence of injury to RJLC's clients or prospective clients is not mitigating because our public interest analysis "focus[es] . . . on the welfare of investors generally and the threat one poses to investors and the markets in the future."[135]

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[134] *Kornman*, 2009 WL 367635, at *9 (internal quotation and citation omitted).

[135] *Kornman*, 2009 WL 367635, at *9; *vFinance Invs., Inc.*, Exchange Act Release No. 62448, 2010 WL 2674858, at *17 (July 2, 2010); *see also Christopher A. Lowry*, Advisers Act Release No. 2052, 2002 WL 1997959, at *5 n.21 (Aug. 30, 2002) (finding that respondent's repayment to clients of funds he diverted from them did not "excuse[] his initial misrepresentations"), *aff'd*, 340 F.3d

Lucia argues that the initial decisions in *Corbin Jones*[136] and *Joseph C. Lavin*[137] demonstrate that investor losses are an important consideration. But these cases are inapposite because they involved findings that the respondents' violations were egregious, in part, because they caused investor losses.[138] While the absence of investor injury is not mitigating, its existence may be considered in determining the egregiousness of the respondent's actions.[139] Here, even without investor injury as an aggravating factor, Lucia's misconduct was egregious and a bar is in the public interest.

As an alternative to a bar, Lucia contends that it would be more appropriate to impose a censure and require undertakings such as "retain[ing] a monitor to ensure that any public presentations he makes do not utilize 'backtests' or hypothetical illustrations of relative strategy performance." Lucia contends that such remedies would be more in line with the lesser reme-

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501 (8th Cir. 2003); *James C. Dawson*, Advisers Act Release No. 3057, 2010 WL 2886183, at *3 (July 23, 2010) (barring respondent in part because his "dishonesty in defrauding his clients breached the trust that is the underpinning of the fiduciary relationship, regardless of whether there was any net loss of money to his clients").

[136] Initial Decision Release No. 568, 2014 WL 668853 (Feb. 21, 2014).

[137] Initial Decision Release No. 373, 2009 WL 613543 (March 10, 2009).

[138] *Jones*, 2014 WL 668853, at *4; *Lavin*, 2009 WL 613543, at *5.

[139] *See, e.g., Dawson*, 2010 WL 2886183, at *3 ("[O]ur finding that Dawson's conduct was egregious is based on the nature of the violation itself, not solely on any calculation of financial harm to his clients.").

dies imposed in seven settled Commission proceedings.[140] But we have repeatedly found that the remedies imposed in settled actions are inappropriate comparisons because pragmatic considerations "such as the avoidance of time-and-manpower-consuming adversary proceedings," justify accepting lesser remedies in settlement.[141] In addition, the appropriate remedy depends on the facts and circumstances presented and cannot be determined precisely by comparison with actions taken in other cases.[142] Here, the alternative remedy that Lucia proposes do not provide

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[140] Lucia cites *New England Inv. and Retirement Group, Inc.*, Advisers Act Release No. 3516, 2012 WL 6591597 (Dec. 18, 2012); *Modern Portfolio Mgmt., Inc.*, Advisers Act Release No. 3702, 2013 WL 5740461 (Oct. 23, 2013); *Equitas Capital Advisors, LLC*, Advisers Act Release No. 3704, 2013 WL 5740460 (Oct. 23, 2013); *Independent Fin. Group*, Advisers Act Release No. 1891, 2000 WL 1121531 (Aug. 8, 2000); *William J. Ferry*, Advisers Act Release No. 1747, 1998 WL 487681 (Aug. 19, 1998); *Meridian Inv. Mgmt. Corp.*, Advisers Act Release No. 1779, 1998 WL 898489 (Dec. 28, 1998); *LBS Capital Mgmt., Inc.*, Advisers Act Release No. 1644, 1997 WL 401055 (July 18, 1997).

[141] *Michael C. Pattison, CPA*, Exchange Act Release No. 67900, 2012 WL 4320146, at *11-12 (Sept. 20, 2012) (quoting *Nassar and Co., Inc.*, 47 SEC 20, 26 & n.37 (1978)); *Ficken*, 2008 WL 4610345, at *4. We also note that settlements are not precedent. *Citizens Capital Corp.*, Exchange Act Release No. 67313, 2012 WL 2499350, at *5 n.27 (June 29, 2012). The remedies imposed on Respondents are amply justified by our findings of violations, as discussed.

[142] *Ficken*, 2008 WL 4610345, at *4; *see also Butz v. Glover Livestock Comm'n Co., Inc.*, 411 U.S. 182, 187 (1973) (holding that a sanction imposed within the authority of an administrative agency is "not rendered invalid in a particular case because it is more severe than sanctions imposed in other cases"); *Geiger v. SEC*, 363 F.3d 481, 488 (D.C. Cir. 2004) (holding that, because the "Commission is not obligated to make its sanctions uniform," the court would not compare the sanctions imposed in the case to those imposed in previous cases).

sufficient protection for investors given the nature of his misconduct and the opportunity that continued association with an investment adviser, broker, or dealer would present for future violations.

Accordingly, we find that it is in the public interest to bar Lucia from associating with any investment adviser, broker, or dealer. A bar will prevent Lucia from putting investors at further risk and serve as a deterrent to others from engaging in similar misconduct.

B. Revocation of Respondents' investment adviser registrations

Under Advisers Act Section 203(e), we may suspend or revoke an investment adviser's registration if we find that (i) the investment adviser, or any person associated with it, willfully violated, or willfully aided and abetted the violation of, any provision of the Advisers Act and (ii) the sanction is in the public interest.[143] We consider the same public interest factors discussed above for determining whether to revoke an investment adviser's registration.[144]

Lucia states in his brief that "he makes no challenge to . . . ordering the registrations of [Respondents] as investment advisers permanently revoked." The evidence amply supports such revocation, for the reasons discussed above, as being necessary to protect the public interest.[145]

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[143] 15 U.S.C. § 80b-3(e).

[144] *See Sherwin Brown*, Advisers Act Release No. 3217, 2011 WL 2433279, at *6 (June 17, 2011).

[145] Again, Lucia's conduct and level of intent are imputed to RJLC.

C. Cease-and-desist orders

Advisers Act Section 203(k) authorizes us to issue cease-and-desist orders for violations of the Advisers Act.[146] Such orders must be in the public interest, which we determine by looking to whether there is some risk of future violation.[147] The risk "need not be very great" and is ordinarily established by a single past violation absent evidence to the contrary.[148] We also consider whether other factors demonstrate a risk of future violations, including the factors discussed above concerning Lucia's bar as well as whether the violation is recent, the degree of harm to investors or the marketplace resulting from the violation, and the remedial function to be served by the cease-and-desist order in the context of any other sanctions being sought.[149] This inquiry is flexible, and no single factor is dispositive.[150]

Here, Respondents' violations, the egregiousness of their misconduct, and the other public interest factors discussed above establish a risk of future violations. Accordingly, we find that it is in the public interest to order Respondents to cease and desist from committing or causing any violations or future violations of Advisers Act Sections 206(1), 206(2), and 206(4) and Rule 206(4)-1.

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[146] 15 U.S.C. § 80b-3(k).

[147] *Robert L. Burns*, Advisers Act Release No. 3260, 2011 WL 3407859, at *8 n.34 (Aug. 5, 2011).

[148] *KPMG Peat Marwick LLP*, Exchange Act Release No. 43862, 2001 WL 47245, at *24 (Jan. 19, 2001), *pet. denied*, 289 F.3d 109 (D.C. Cir. 2002).

[149] *Id.* at *26.

[150] *Id.*

D. Civil penalties

We may impose civil penalties under Advisers Act Section 203(i) if we find that Respondents willfully violated the Advisers Act and such penalties are in the public interest.[151] Both factors are satisfied here. Respondents repeatedly made fraudulent misstatements and omissions in willful violation of the Advisers Act and their fiduciary duties. Their conduct was egregious and thus warrants the imposition of penalties as a deterrent to Respondents and others against committing similar violations. Such considerations are not outweighed by Respondents' clean disciplinary history or the lack of evidence concerning investor loss or unjust enrichment.

Also, because Respondents' violations involved fraud and were in reckless disregard of a regulatory requirement, we find that second-tier penalties are warranted.[152] Therefore, because the amounts imposed by the ALJ ($250,000 upon RJLC and $50,000

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[151] 15 U.S.C. § 80b-3(i). In determining whether penalties are in the public interest, we consider: (i) whether the act or omission involved fraud; (ii) whether the act or omission resulted in harm to others; (iii) the extent to which any person was unjustly enriched; (iv) whether the individual has committed previous violations; (v) the need to deter such person and others from committing violations; and (vi) such other matters as justice may require. *Id.*

[152] Section 203(i) establishes a three-tier system for calculating penalties: (i) first-tier penalties are permissible for securities law violations; (ii) second-tier penalties are permissible for securities law violations involving "fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement"; and (iii) third-tier penalties are permissible for violations that satisfy the second-tier penalty requirements and "directly or indirectly resulted in substantial losses or created significant risk of sub-

upon Lucia) are within the permissible second-tier range,[153] and are in the public interest, we grant the Division's request and impose those same amounts upon Respondents.[154]

Respondents contend that penalties are unwarranted against RJLC because it has no assets or operations, is no longer registered as an investment adviser, and is a dormant corporate shell. Respondents also contend that imposing an uncollectable penalty against RJLC will prejudice Lucia without any benefit to the public interest. These contentions are meritless. If RJLC lacked the ability to pay penalties, it

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stantial losses to other persons or resulted in substantial pecuniary gain to the person who committed the act or omission." *Id.*; 17 C.F.R. § 201.1004.

[153] The maximum second-tier penalty the Commission could impose for a single act of misconduct is $375,000 for RJLC and $75,000 for Lucia. 17 C.F.R. § 201.1004 & Pt. 201, Subpt. E, Tbl. IV.

[154] Although the amounts imposed by the ALJ are within the second-tier range, he categorized them as third-tier penalties. We find that this categorization was unwarranted because the Division did not establish: (i) that Respondents' clients or prospective clients suffered any losses or were at significant risk of suffering substantial losses or (ii) whether Respondents' gain from the fraud was substantial. For the latter consideration, while the Division introduced evidence showing that Respondents' business was profitable, it did not demonstrate the extent to which Respondents' misconduct was responsible for that profit. In any event, we find that the amounts imposed are warranted as second-tier penalties for the reasons discussed above.

was required under Commission Rule 630(a) to present evidence thereof.[155] It has failed to do so.[156] Respondents also have not explained how Lucia would be prejudiced if we order RJLC to pay penalties.

Accordingly, we find that it is in the public interest to impose second-tier penalties of $250,000 upon RJLC and $50,000 upon Lucia.

An appropriate order will issue.[157]

By the Commission (Chair WHITE and Commissioners AGUILAR and STEIN); Commissioners GALLAGHER and PIWOWAR, dissenting. A dissenting opinion will issue separately.

Brent J. Fields
Secretary

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[155] 17 C.F.R. § 201.630(a).

[156] Respondents also have waived their right to assert the defense of inability to pay because they did not raise the issue before the ALJ. *David Henry Disraeli*, Advisers Act Release No. 2686, 2007 WL 4481515, at *19 (Dec. 21, 2007), *aff'd*, 334 F. App'x 334 (D.C. Cir. 2009).

[157] We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 75837 / September 3, 2015

INVESTMENT ADVISERS ACT OF 1940
Release No. 4190 / September 3, 2015

INVESTMENT COMPANY ACT OF 1940
Release No. 31806 / September 3, 2015

Admin. Proc. File No. 3-15006

In the Matter of

RAYMOND J. LUCIA COMPANIES, INC.
and
RAYMOND J. LUCIA, SR.

ORDER IMPOSING REMEDIAL SANCTIONS

On the basis of the Commission's opinion issued this day, it is

ORDERED that Raymond J. Lucia, Sr. be barred from association with any investment adviser, broker, or dealer; and it is further

ORDERED that the investment adviser registrations of Raymond J. Lucia Companies, Inc. and Raymond J. Lucia, Sr. are revoked; and it is further

ORDERED that Raymond J. Lucia Companies, Inc. and Raymond J. Lucia, Sr. cease and desist from committing or causing any violations or future violations of Sections 206(1), 206(2), and 206(4) of the Investment Advisers Act of 1940 and Rule 206(4)-1; and it is further

ORDERED that Raymond J. Lucia Companies,

Inc. pay a civil money penalty of $250,000; and it is further

ORDERED that Raymond J. Lucia, Sr. pay a civil money penalty of $50,000.

Payment of the civil money penalty shall be (i) made by United States postal money order, certified check, bank cashier's check, or bank money order; (ii) made payable to the Securities and Exchange Commission; (iii) mailed to Enterprises Services Center, Accounts Receivable Branch, HQ Bldg., Room 181, 6500 South MacArthur Blvd., Oklahoma City, OK 73169; and (iv) submitted under cover letter that identifies the respondent and the file number of this proceeding.

By the Commission.

Brent J. Fields
Secretary

APPENDIX D

Opinion of Commissioner Gallagher and Commissioner Piwowar, dissenting from the opinion of the Commission

Commissioner Daniel M. Gallagher and Commissioner Michael S. Piwowar

Oct. 2, 2015

The misdeeds of the respondents in this case have been well established.[1] In making pitches for investment advisory services to large audiences on multiple occasions, the respondents touted an approach called "Buckets of Money," a catchy name for a re-balancing strategy. Unfortunately, the Commission majority has taken a relatively straightforward set of facts and needlessly engaged in "rulemaking by opinion." For that reason, we dissent from the majority opinion.

The respondents claimed that their approach was more likely to produce favorable results when compared to a conservative portfolio of 100% bonds, an aggressive portfolio of 100% stocks, and a hybrid portfolio of 60% stocks and 40% bonds. The respondents tried to demonstrate the superiority of their "Buckets of Money" approach using scenarios from 1973, when the stock market dropped significantly for two years, and from 1966, when the Dow Jones Industrial Average stagnated for a sixteen year period, as compared to the three other portfolios.

The problem for the respondents was that (i) they did not actually utilize the "Buckets of Money" approach in determining the results for in the 1973 and 1966 scenarios and (ii) with respect to the 1973 scenario,

they could not even re-construct their supporting calculations. Had the Commission majority simply stopped there, the opinion would have been easy to support.

Instead, the majority opinion creates from whole cloth specific requirements for advertisements that include the word "backtest." Despite the lack of any statutory or regulatory definition of what constitutes a "backtest," the majority opinion finds it fraudulent or deceptive practice if a backtest fails to use actual historical rates — even if the slideshow presentation specifically discloses the use of assumed rates for certain components.

In the context of the respondents' slideshow presentation, the use of the word "backtest" and assumed inflation rates were not misleading. A review of the slideshow reveals that the respondents were making two points: (i) inflation can cause a retiree to exhaust retirement savings; and (ii) stock returns can be volatile and a significant decline in the first year or two of retirement will affect how long retirement savings will last.

To illustrate how inflation can affect retirement savings, the respondents used a 3% assumed inflation rate. The effect of inflation was first presented in connection with the conservative scenario. Using the 3% assumed inflation rate, the respondents created a baseline scenario indicating that the conservative portfolio would be exhausted in 27 years if withdrawals were indexed for inflation.

In contrast, the respondents presented the results of an aggressive portfolio invested 100% in stocks. Using an assumed annual return of 10%, the respondents

stated that the aggressive portfolio would never be exhausted. However, the respondents' slideshow presentation repeatedly cautioned that stock returns can be highly volatile and that a significant decline in stocks during the first year or two of retirement could affect whether retirement savings will be sufficient.

The respondents used the 1973 bear market scenario to show the possible effects of stock market volatility on retirement savings and comparative outcomes among the aggressive, hybrid, and "Buckets of Money" portfolios.[2] Using the 3% assumed inflation rate, the respondents claimed in the 1973 scenario that the aggressive portfolio was exhausted in 17 years and the hybrid portfolio was exhausted in 21 years. On the other hand, the respondents asserted that the "Buckets of Money" portfolio would not run out of funds.[3]

It is appropriate to use a consistent, assumed inflation rate when comparing the results among portfolios. Moreover, we find troubling the majority opinion's holding that, notwithstanding the disclosure that the scenarios were determined using assumed 3% inflation, the slideshow presentation was nonetheless fraudulent because a backtest must use historical inflation rates.

The majority opinion emphasizes the testimony of witnesses at the slideshow presentations who thought that the backtests used actual historical inflation rates. But the test for materiality is an objective, not subjective, test of the reasonable investor. Given the clear disclosure of the inflation rate assumptions in the slideshow presentation, we find that a reasonable investor would not have believed that actual historical rates of inflation were used in the backtests.

Finally, the respondents have raised important issues with respect to whether the administrative law judge[4] overseeing the proceeding was appointed in a manner consistent with the Appointments Clause of the Constitution. Even though the Commission is free to express its views on Constitutional issues, we recognize and believe it is appropriate that Article III federal judges ultimately resolve this issue.[5]

[1] *In the Matter of Raymond J. Lucia Companies, Inc. and Raymond J. Lucia, Sr.*, Securities Exchange Act Release No. 75837 (Sept. 3, 2015), available at http://www.sec.gov/litigation/opinions/2015/34-75837.pdf.

[2] The respondents asserted that had a person retired in 1973, stock returns for the next two years declined by 41.13%. The respondents showed other slides analyzing similar effects from 1966, when the Dow Jones Industrial Average began and ended for a sixteen year period at around 1,000 points.

[3] As noted previously, the purported results of the Buckets of Money portfolio for the 1973 scenario were fraudulent, but were fraudulent for reasons unrelated to the use of an assumed rate of inflation.

[4] Before the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), Commission leadership actively sought from Congress expanded authority to seek monetary penalties against individuals through administrative proceedings. The result was Section 929P of Dodd-Frank. *See* SEC's "Wish List" of 42 Changes It Seeks in the Federal Securities Laws (July 16, 2009), available at http://www.securitiesdocket.com/2009/07/16/sec-s-wish-list-of-42-changes-it-seeks-in-the-federal-securities-laws/ (citing Fox Business reports).

[5] *See* Duka v. SEC, 2015 WL 4940057 (S.D.N.Y. Aug. 3, 2015); Hill v. SEC, 2015 WL 4307088 (N.D. Ga. June 8, 2015).

Modified: Oct. 2, 2015

APPENDIX E

INITIAL DECISION
RELEASE NO. 540
ADMINISTRATIVE
PROCEEDING
FILE NO. 3-15006

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

In the Matter of RAYMOND J. LUCIA COMPANIES, INC. and RAYMOND J. LUCIA, SR.	INITIAL DECISION ON REMAND December 6, 2013

* * *

BEFORE: Cameron Elliot, Administrative Law Judge

SUMMARY

This Initial Decision on Remand supplements the July 8, 2013, Initial Decision in this proceeding, confirms that Respondent Raymond J. Lucia Companies, Inc. (RJLC), violated Sections 206(1), 206(2), and 206(4) of the Investment Advisers Act of 1940 (Advisers Act) by misrepresenting the validity of purported backtesting in seminars for prospective investors, and that Respondent Raymond J. Lucia, Sr. (Lucia) aided and abetted RJLC's violations of Sections 206(1),

206(2), and 206(4) of the Advisers Act, and bars Lucia from associating with an investment adviser, broker, or dealer, revokes Lucia's and RJLC's investment adviser registrations, imposes a civil penalty of $50,000 on Lucia and $250,000 on RJLC, and orders Lucia and RJLC to cease and desist from further violations of the Advisers Act.

I. INTRODUCTION

A. Procedural Background

The Securities and Exchange Commission (Commission) issued its Order Instituting Administrative and Cease-and-Desist Proceedings (OIP) on September 5, 2012, pursuant to Section 15(b) of the Securities Exchange Act of 1934 (Exchange Act), Sections 203(e), 203(f), and 203(k) of the Advisers Act, and Section 9(b) of the Investment Company Act of 1940 (Investment Company Act). Lucia and RJLC filed their Answers on September 19, 2012.[1]

The parties filed their prehearing briefs by November 5, 2012. A hearing was held on November 8-9, 13-14, 19-21, 2012, and December 17-18, 2012, at the Commission's headquarters in Washington, D.C. The admitted exhibits are listed in the Record Index issued by the Secretary of the Commission on April 19, 2013.[2] The Division of Enforcement (Division) and

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[1] Lucia and RJLC filed separate Answers, but they are substantively identical. Lucia and RJLC presented a unified defense and, where appropriate, are referred to collectively as Respondents.

[2] On April 12, 2013, counsel for Respondents offered a Submission of Recent Decision (Submission) to demonstrate the "realities and inherent difficulties in ascertaining the value of REIT shares." The Submission also offered an excerpt of the 2014 Budget of the Federal Government to support their arguments

Lucia thereafter filed post-hearing briefs and post-hearing reply briefs.[3]

On July 8, 2013, I issued an Initial Decision finding that RJLC violated, and Lucia aided and abetted RJLC's violations of, Sections 206(1), 206(2), and 206(4) of the Advisers Act by fraudulent misrepresentations concerning an investment strategy involving Real Estate Investment Trust (REIT) securities. The Commission had alleged three other misrepresentations in the OIP, namely, the use of a misleading inflation rate, failure to deduct fees or disclose that the backtests were not net of fees, and failure to reallocate assets in accordance with the strategy presented, without disclosing that failure. I found in the July 8, 2013, Initial Decision that these additional misrepresentations, even if true, would not have resulted in different sanctions than those imposed for misrepresentations regarding REITs. Accordingly, I declined to analyze the three other misrepresentations alleged in the OIP.

On July 18, 2013, RJLC and Lucia filed a Motion to Correct Manifest Errors of Fact, pursuant to Rule 111(h) of the Commission's Rules of Practice. See 17

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regarding inflation rates. I admitted the decision and excerpt as part of the official record.

[3] Citations to the transcript of the hearing are noted as "Tr. ___.". Citations to Lucia's Answer are noted as "Lucia Answer ___," and to RJLC's Answer as "RJLC Answer ___." Citations to exhibits offered by the Division and Respondents are noted as "Div. Ex. ___." and "Resp. Ex. ___.", respectively. The Division's and Respondents' post-hearing briefs are noted as "Div. Br. ___." and "Resp. Br. ___.", respectively. The Division's and Respondents' post-hearing reply briefs are noted as "Div. Reply ___" and "Resp. Reply ___," respectively. The Division's and Respondents' pre-hearing briefs are noted as "Div. Pr. H Br. ___." and "Resp. Pr. H Br. ___.", respectively.

C.F.R. § 201.111(h). On August 7, 2013, I issued an Order on Motion to Correct Manifest Errors of Fact which updated the Initial Decision to correct certain errors. Those corrections are reflected herein.

On August 8, 2013, the Commission, on its own initiative, remanded the case for findings as to the three additional alleged misrepresentations. Raymond J. Lucia Cos., (Aug. 8, 2013) (unpublished Order Remanding Case for Issuance of Initial Decision Pursuant to Rule of Practice 360) (Remand Order). This Initial Decision on Remand updates the July 8, 2013, Initial Decision by making findings as to the remaining allegations. In accordance with the Remand Order, I have considered the specific facts and circumstances presented by the three additional alleged misrepresentations. The sanction determinations made in the July 8, 2013, Initial Decision remain appropriate, for the reasons explained infra.

B. Summary of Allegations

The instant proceeding concerns alleged misrepresentations of backtested returns of fictional investment portfolios using Lucia and RJLC's proprietary Buckets of Money® (BOM) strategy. OIP, p. 2. The OIP alleges the misleading application of (i) historical inflation rates, (ii) investment adviser fee impact, (iii) returns on REITs, and (iv) reallocation of assets in fictional backtested portfolios utilizing the BOM strategy, in slideshow presentations offered by Lucia and books authored by Lucia, a registered investment adviser, and RJLC, a previously registered investment adviser, located in San Diego, California. OIP, p. 2. The OIP alleges that RJLC violated Sections 206(1), 206(2), and 206(4) of the Advisers Act and Rule 206(4)-1(a)(5) thereunder; Lucia aided and abetted and

caused RJLC's violations of Sections 206(1), 206(2), and 206(4) and Rule 206(4)-1(a)(5) thereunder by knowingly or recklessly misrepresenting the accuracy of the backtested investment portfolios to prospective investment clients; and RJLC violated Section 204 of the Advisers Act and Rule 204-2(a)(16) thereunder by failing to maintain proper books and records. OIP, pp. 9-10.

Lucia and RJLC deny most of the key allegations. Lucia Answer, pp. 3-7; RJLC Answer, pp. 3-7. Lucia and RJLC deny that the BOM slideshow presentations were misleading and deny that their backtests were misleading due to their use of a 3% inflation rate, their failure to consider investment adviser fees, their use of assumed REIT rates, and their failure to reallocate assets after a certain period. Lucia Answer, pp. 3-7; RJLC Answer, pp. 3-7.

II. FINDINGS OF FACT

The findings and conclusions herein are based on the entire record. I applied preponderance of the evidence as the standard of proof. See Steadman v. SEC, 450 U.S. 91, 102 (1981). I have considered and rejected all arguments, proposed findings, and conclusions that are inconsistent with this Initial Decision on Remand.

A. Background

1. Lucia

Lucia, at the time of the OIP, was a 61-year old registered investment adviser and the sole owner of

RJLC. Lucia Answer, pp. 1-2.[4] Lucia began his financial management career in 1974 as an insurance agent with Penn Mutual Insurance Company, which he left in 1991. Tr. 1031. Afterward, Lucia was self-employed for a few months before joining John Hancock as a general agent. Tr. 1033-34. Lucia left John Hancock in 1995 and joined Acacia Life Insurance Company. Tr. 1034. In 1996, Lucia registered with the Commission as an investment adviser, associated with RJLC, which registered as an investment adviser in 2002. RJLC Answer, p. 1; Div. Ex. 2, p. 5; Tr. 1035.

Lucia has hosted the *Ray Lucia Show* on the radio since 1990, and the show became nationally syndicated in 2000. Tr. 1025-26. In 2010, the BIZ Network began televising the *Ray Lucia Show*. Tr. 1025-26. Lucia has authored three books promoting the BOM strategy–Buckets of Money: How to Retire in Comfort and Safety (2004); Ready...Set...Retire! (2007); and The Buckets of Money Retirement Solution: The Ultimate Guide to Income for Life (2010). Lucia also used two websites, www.rjlwm.com and www.raylucia.com, for marketing, and posted some of his seminars on the latter. Tr. 624; Lucia Answer, p. 2.

Until June 2010, Lucia was the sole owner of RJLC. Lucia Answer, pp. 1-2. Lucia was also sole owner of a network of financial companies associated with RJLC. Id., p. 1-2; Tr. 516. In addition to being

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[4] Lucia attended Palomar Junior College for a year and a half, beginning in 1967, Western Illinois University between 1968 and 1969, and San Diego State between 1969 and 1970. Tr. 1030. He received a bachelor's degree from United States International University in 1971. Tr. 1030. Lucia received a Series 7 license in 1983, a Series 24 license in 1997, a Certified Financial Planner designation in 1988, and a Series 63 license in 2002. Tr. 1032-35.

sole owner of RJLC, Lucia owned Lucia Financial, LLC (Lucia Financial), a registered broker-dealer for RJLC; owned RJL Enterprises, Inc., Lucia's media company; and partially owned LLK Insurance Services, LLC. Tr. 73, 516; Div. Ex. 2, p. 4. Lucia collected income from RJLC through Ray Sr. Sole Proprietor. Tr. 517.

2. RJLC

Lucia founded RJLC in 1994, and between 2006 and 2010, RJLC operated under the business name RJL Wealth Management. RJLC Answer, p. 1; Tr. 1026-27; Div. Ex. 2, p. 4, n.4. Between 2002 and 2011, RJLC was a registered investment adviser. Lucia Answer, p. 1; RJLC Answer, p. 1. RJLC had an investment committee, which performed diligence on proposed products and approved products that RJLC-affiliated advisors could sell.[5] Tr. 1301, 1569-70. Lucia and his son, Ray Lucia, Jr. (Lucia, Jr.) were members of the investment committee. Tr. 1076-77, 1301. Lucia, Jr. now operates RJL Wealth Management, LLC (RJLWM), a registered investment adviser and partial successor to RJLC. Tr. 1233-34; Lucia Answer, p. 1.

Between 2002 and 2007, RJLC had a network agreement with Securities America. Tr. 474, 1475, 1601. Lucia and Securities America jointly owned an investment adviser, RJL Financial Network, which

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[5] RJLC as an investment adviser did not directly sell securities. The securities were sold through the broker-dealer arm of RJLC's affiliated broker-dealers, Securities America, Inc. (Securities America), and later, First Allied Securities, Inc. (First Allied). Tr. 476, 502. The advisors would make the recommendations, and then execute the sales through the affiliate broker, with whom the registered representatives had independent contractor agreements. Tr. 476, 502.

operated as a joint business development effort to handle leads generated from Lucia's slideshow presentations. Tr. 446-47. Investment advisers for the joint venture, including Lucia, were registered representatives of both RJLC and Securities America. Tr. 475-76. Fees generated through the investment advisers were split between RJLC and Securities America, depending upon the source of the lead. Tr. 502. Lucia generated most, if not all, of the leads. Tr. 1075. Securities America reviewed marketing and advertising generated by Lucia and RJLC before public distribution, including radio and television spots and the slideshow presentations given by Lucia. Tr. 564-65, 683, 694; Resp. Ex. 20.

In 2007, RJLC and Securities America ended their network agreement. Tr. 474. Although there were apparently multiple reasons for the split between the companies, one such reason was an unfavorable audit of RJLC by Securities America in summer 2007. Tr. 454-60. At least one of the subjects of the audit was the BOM strategy; Theresa Ochs (Ochs), Securities America's relationship manager with RJLC, provided marketing materials to the auditors, including a booklet on the "bucket strategy," and answered auditors' questions about marketing materials. Tr. 456-58. In particular, Securities America had previously asked RJLC for the basis of its claimed REIT returns. Tr. 566. Ultimately, the chief compliance officer of Securities America told Ochs, who later became RJLC's chief compliance officer, that he would "make it very difficult" for Lucia to stay associated with Securities America. Tr. 460-61, 467-68. Following its split from Securities America, in 2007, RJLC entered into a similar networking agreement with First Allied, which lasted until 2011. Tr. 1475. Like Securities America,

First Allied reviewed advertisements, including television and radio spots, and marketing materials, including the slideshow presentation at issue, from a compliance perspective. Tr. 527-30; Div. Exs. 24-49; Resp. Exs. 25-29.

3. RJLC's Business Model

The Lucia family of companies has been very successful: it employed about eight people in 2000, and grew to employ 100 at the time of the hearing, with gross revenue of close to $20 million. Tr. 1220, 1347, 1693. In 2010, RJLWM employed forty-three investment adviser representatives and operated thirteen offices nationwide. Div. Ex. 2, p. 4. During the period between January 1, 2009, and January 31, 2010, RJLC and Lucia Financial generated a combined gross income of $14.1 million, of which RJLC registered representatives (including Lucia and Lucia, Jr.) generated advisory fees of approximately $1.7 million. Div. Ex. 4, p. 8; Tr. 1660. RJLC earned most of its investment adviser revenue by collecting fees for assets under management, but this constituted a paltry fraction of revenues in comparison with the commissions generated through sales of securities through affiliated brokers. Tr. 492, 1656; Div. Ex. 2, p. 7.[6] As of early 2010, RJLC had approximately 4,700 active accounts and $300 million in assets under management. Div. Ex. 2, p. 6; Tr. 491-92.

Sales of securities through RJLC's affiliated brokers were Respondents' main income generator. Between January 1, 2009, and January 31, 2010, Re-

[6] It also earned revenue for hourly charges, fixed-fee consulting arrangements, and management fees for wrap programs it co-sponsored. Tr. 492-93, 517.

spondents collected $12.4 million in gross commissions from sales of securities through First Allied, $8.7 million of which was paid to Lucia as commissions on the sale of non-traded REITs – undoubtedly the biggest revenue generator for Respondents during that period. Div. Ex. 2, p. 7; Div. Ex. 4, p. 8; Tr. 104, 1349. Through RJLC-affiliated representatives, RJLC clients invested more than $143 million in non-traded REITs during the same period. Div. Ex. 4, p. 8; Tr. 506. Of the $12.4 million in gross commissions from sales of securities, RJLC paid $2.7 million, or approximately 22%, to its registered representatives.[7] Div. Ex. 4, p. 8.

Lucia and Lucia, Jr. unconvincingly tried to downplay the importance of REITs to their bottom lines. Lucia reasoned that REITs generate a one-time fee, unlike other products, which continue to generate fees over time. Tr. 1348. Lucia was paid from his sole proprietorship, rather than from any one of his family of companies, and he paid much of the overhead of those companies, including salary, marketing, travel, and general office expenses. Tr. 1349, 1352, 1657. That is, Lucia's $8.7 million in gross commissions was not his actual take-home pay, and there have been years when his tax returns have shown a loss of close to $1 million. Tr. 1347, 1349. Lucia, Jr. emphasized that the revenues reported in the examination reports (Div. Exs. 2 and 4) were merely gross revenues, and did not account for expenses. Tr. 1661-62. He also testified that in 2011, which was a "transition year" in which revenues were down to about $16 million, the

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[7] RJLC used to pay its advisors based upon a percentage of sales commissions and fees, but in 2011, it moved to an all-salary employment model. Tr. 502, 1076-77, 1569.

Lucia family of companies lost $2 million. Tr. 1693-94.

Although I have no reason to doubt that Respondents have had good years and bad years, the Lucia family of companies are, overall, highly profitable, and Respondents have done very well for themselves, in part through their seminars. According to Lucia, Jr., August 2012 was a "record month," with $1.6 million in gross revenues. Tr. 1655. In 2011, the family of companies, despite the reported loss of $2 million, was still successful enough that Lucia, Jr. paid himself a $325,000 salary and took ownership withdrawals of "a couple hundred thousand" more, for a total of "about half a million dollars." Tr. 1694, 1701. Lucia, too, continues to collect a $300,000 salary from RJLWM in addition to fees for leads and a markup on advertisement sales on his show, $1.8 million of which came from RJLWM. Tr. 1025, 1697-99. Lucia admitted that there have been years when he has made $1 million. Tr. 1347.

More importantly, REITs generated "a high percentage of the revenue" for Respondents. Tr. 1347-48. Even assuming REITs generated the smallest profit margin of all the products sold, REITs were the clear moneymaker for RJLC (and RJLWM). According to Lucia, Jr., expenses in 2010 were "seven to eight million dollars a year plus rep comp and bonuses." Tr. 1661. As noted, representative compensation and bonuses were $2.7 million for January 2009 through January 2010. Div. Ex. 4, p. 8. Thus, total expenses for 2010 were at most approximately $10.7 million, compared to $12.4 million in gross commissions alone, leaving Lucia and RJLC with a substantial profit. Indeed, about 70% of gross commissions ($8.7 million) came from sales of non-traded REITs, which are by

themselves adequate to cover all overhead except compensation for registered representatives. Overall, therefore, non-traded REITs have been very important, even crucial, to Respondents' profitability, and Respondents possess and have possessed an overwhelming incentive to sell as many of them as possible.

4. Lucia Financial

Lucia Financial was a registered broker-dealer, wholly owned by Lucia. Tr. 73, 469. Lucia Financial acted as a "limited use" broker-dealer for RJLC, maintaining no client accounts. Tr. 471-72. Lucia Financial's sole purpose was to collect revenue from marketing reimbursements and marketing revenues paid to Lucia and RJLC. Tr. 472-74. Issuers of non-traded REITs paid marketing reimbursements to Lucia for hosting seminars on those products. Tr. 474. Marketing revenues were a portion of distribution fees earned through sales of non-traded REITs by advisors registered with First Allied (and previously Securities America) and RJLC. Tr. 474. Between January 1, 2009, and January 1, 2010, Lucia Financial collected $1,140,151 in marketing reimbursements and marketing revenue, 96% of which came from just four REIT issuers. Div. Ex. 4, p. 5; Div. Ex. 52.

5. Sale of RJLC and Lucia Financial

Citing his interest in devoting more time to his media career, in April 2010, Lucia sold RJLC's client accounts, as well as Lucia Financial's brokerage business, to his son, Lucia, Jr. Tr. 507-10, 1027. Following the sale, and beginning in June 2010, Lucia, Jr. wholly owned the registered investment adviser RJLWM, with the client accounts purchased from RJLC. Tr. 587, 1027. Additionally, Lucia, Jr. created

Lucia Securities, LLC (Lucia Securities), to take over the brokerage business from Lucia Financial and act as broker-dealer to RJLWM. Tr. 469, 587-89. Lucia maintains active involvement with RJLWM, including his investment adviser registration. Tr. 1024.

B. Buckets of Money

Lucia developed the BOM strategy in the mid-1990s, trademarking the term in 2000. Tr. 1037, 1046. After years of difficulty protecting the BOM trademark, in 2011 Lucia rebranded the strategy The Bucket Strategy®. Tr. 1047.

In its simplest terms, the BOM strategy advocates spending income and principal from safe assets prior to depleting riskier assets in a portfolio, giving the riskier assets sufficient time to grow, and lengthening the lifespan of investors' nest eggs.[8] Tr. 75, 800, 1055; Div. Ex. 1, p. 179.[9] Lucia based the strategy, in part,

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[8] The parties dispute the precise nature of the BOM strategy. The Division asserts that it "involves allocating a client's assets among three 'buckets,'" that is, it is an asset allocation strategy. Div. Br., p. 6. Respondents assert that it is a "retirement asset withdrawal strategy," and is neither a "model portfolio" nor an asset allocation strategy. Resp. Br., p. 30; Resp. Reply, p. 2. It is not necessary to resolve this issue, because the outcome would be the same however the BOM strategy is characterized. Accordingly, I assume without deciding that Respondents' characterization is the correct one.

[9] Div. Ex. 1, which is the same as Resp. Ex. 3, was produced by Respondents during a 2010 examination by the Commission's Office of Compliance Inspections and Examinations (OCIE). Tr. 68, 86. It is a version of the slideshow Lucia used during his seminars no earlier than March 1, 2009, and was apparently the most recent version of the slideshow provided during the 2010 examination of Respondents. Tr. 86, 582. Because Div. Ex. 1 is not paginated, the cited page numbers are the last three numbers of one of the Bates numbers on the exhibit, SEC-LA3937-

on information he learned after reading a 1998 article by John Bowen, Jr., in the journal Financial Planning, which advocated the idea of withdrawing income from less volatile assets before withdrawing income from more volatile assets. Tr. 1037, 1044-45.

Lucia presented BOM as a retirement strategy, touting its ability to ensure long-term, inflation-adjusted income.[10] Tr. 1055, 1073. A common marketing phrase used by Lucia was "aim to retire in comfort and safety." Tr. 347, 1082. Lucia offered, and RJLC advisors provided, free BOM plans for prospective investors, and the plans could include investment assets already held, proposed investments, or a combination of both. Tr. 729-30, 1068.

A typical "bucket" strategy consists of three buckets of assets, though it could involve more if necessary. Tr. 75, 610-15. The first bucket holds low-risk, liquid assets, such as certificates of deposit, structured notes, treasury notes, investment contracts, or other cash-equivalent investments. Tr. 727-28. Lucia encourages spending bucket one assets and the income generated from them before assets in either the second or the third bucket are used. Tr. 610-15. The second and third buckets contained progressively riskier assets; typically bonds and structured notes in the second, and stocks and REITs in the third. Tr. 728-29.

00XYZ, thus: "Div. Ex. 1, p. XYZ." For ease of reference, I cite only to the Division's exhibit. By contrast, Div. Ex. 21 is the version of the slideshow used during the 2003 Commission examination, discussed infra. Tr. 1484.

[10] Lucia and Richard Plum (Plum), an employee of RJLC who assisted in creating the backtests, testified that the strategy could be tailored to investors at any life stage. Tr. 908, 1056-57. However, retirees and near-retirees were the target audience. Tr. 1060.

RJLC did not typically manage first or second bucket assets. Tr. 727-28. RJLC managed at least a portion of third-bucket category assets for a majority of its customers. Tr. 729.

Lucia introduced BOM in his slideshow presentations, in his books, and on his website as a "time-tested" strategy based upon "empirical evidence" and "science, not art." Div. Exs. 10, 16; Tr. 624-25, 1050, 1111. Lucia also frequently referred to it as a "backtested" strategy. Div. Ex. 1, pp. 437, 467; Div. Ex. 50, p. 22; Div. Ex. 66, p. 47.

C. The BOM Seminars

The BOM seminars are the nucleus of Lucia's business. Lucia marketed his BOM strategy through free slideshow presentation seminars to prospective investors in cities across the country. Tr. 629-30, 1071; Div. Ex. 18. Lucia traveled to multiple cities every year, giving approximately forty BOM seminar presentations per year. Div. Ex. 18; Tr. 1070. Between March and May 2009, for example, Lucia listed on his website fifteen planned seminars throughout the country. Div. Ex. 27. The venues varied, but each typically held a few hundred people. Tr. 1061. Lucia estimates that he has given his BOM slideshow presentation to 50,000 people. Tr. 1061. The presentation included a series of PowerPoint slides, mainly introduced by Lucia, followed by, or preceded by, audience questions. Tr. 1066. Associates of Lucia, including Plum, would often attend the seminars and help field questions from audience members. Tr. 734, 736.

The purpose of these slideshows was to generate leads for RJLC, and now for RJLWM. Tr. 526, 1075. At the end of every presentation, Lucia handed out

contact cards, which attendees filled out and returned to Lucia and his associates. Tr. 279, 378, 436. RJLC's investment advisers followed up on those leads, offering a free BOM consultation. Tr. 1068, 1559. RJLC only made money if the seminar attendees met with an RJLC investment adviser, received the free BOM consultation, and then either purchased investment products through RJLC or opted to have an RJLC advisor manage a portion of the investor's portfolio. Tr. 1067-68.

D. The BOM Slideshow

At the heart of this proceeding is Lucia's BOM slideshow presentation that Lucia gave at his BOM seminars. Lucia has been giving a variation of the slideshow presentation since around 2000. Tr. 672. He has amended the slides over time, but the principles and the progression of the message have remained largely the same. Tr. 834-36; see also Div. Ex. 1 (2009 version of the slideshow); cf. Div. Ex. 21 (2003 version of the slideshow). Of the 126 slides in the slideshow, the first fifteen slides are focused upon investment concerns and goals, and another thirty-nine focus upon Lucia's confrontation of conventional investment wisdom and strategies. Div. Ex. 1. Lucia then progresses through a series of fictional investor portfolios to validate his strategy. Div. Ex. 1. After the fictional investors, Lucia introduces the BOM strategy and his backtests, twenty-seven and eighteen slides, respectively. Div. Ex. 1. Lucia is responsible for, and approves the content of, the slideshow. Tr. 572, 834, 1066-67.

1. The Fictional Investors

Suitably named fictional investors each start with $1 million in retirement savings, require $60,000 a

year in inflation-indexed income, and aspire to bequeath $1 million to their children. Div. Ex. 1, p. 420. The first three fictional investors, comprising twenty-one slides, are subjected to what Lucia asserts are the pitfalls of conventional investment strategies.

a. The "Conservative Campbells"

The risk averse Conservative Campbells invest only in low-risk instruments, including certificates of deposit, individual bonds, and Ginny Maes (securities issued by the National Government Mortgage Association). Id., p. 421. The Campbells' investments are considered "safe & guaranteed." Id. The Campbells' income withdrawals are not indexed for inflation, so even though they are able to withdraw $60,000 a year, over the course of decades, their purchasing power diminishes. Id., p. 422. Assuming the Campbells passed away after thirty years, their $1 million principal investments would still be worth $1 million, but assuming inflation, their principal sees its purchasing power diminish by more than half. Id., p. 423.

b. The "High Rolling Hendersons"

The risk tolerant High Rolling Hendersons invest 100% of their retirement savings in the stock market. Id., p. 427. If the Hendersons enjoyed a flat 10% return from the stock market every year, their portfolio would be worth $4,203,320 in thirty years. Id., p. 427. That total allows for an inflation-indexed withdrawal of $60,000 a year. Id., p. 427. Lucia criticizes such a strategy, however, because, as the slideshow presents, if the Hendersons had retired in 1973, right before the nadir of that period's "Grizzly Bear Market" (Grizzly Bear Market), they would have gone bankrupt within seventeen years. Id., p. 432.

c. The "Balanced Buttafuccos"

The Balanced Buttafuccos, who invested in a balanced portfolio of 40% bonds and 60% stock, are also subjected to a retirement date of January 1, 1973, leading into the Grizzly Bear Market. Id., p. 435. They enjoy income for only twenty-one years, until completely depleting their portfolio. Id., p. 436. The Buttafuccos' 60/40 stock and bond mix is what Lucia uses as a proxy for the industry standard balanced portfolio he frequently denigrates. Id., p. 437; Tr. 1272. The slideshow suggests that the Buttafuccos are the main comparator to Lucia's "bucketized" investors. Div. Ex. 1, p. 437. The Buttafuccos' results were described as "backtested." Id., p. 437.

d. The "Bold Bucketeers"

As a contrast to the three previous fictional investors, the slideshow next introduces the Bold Bucketeers, the first investors in the slideshow to structure a portfolio around BOM principles, and also the first fictional investors to invest in REITs. Id., pp. 439, 449. Having the same initial resources and goals as the three previous investors, the Bucketeers employ a three-bucket strategy, with the addition of REITs. Id., p. 465. The portfolio contains 40% stocks, 20% REITs, and 40% bonds–referred to in testimony as a "40-20-40" strategy. Id., p. 465; Tr. 780, 806-07. $200,000 is invested in REITs, which produce an assumed dividend rate of 7.75% per year, and $400,000 in stocks, which grow at an assumed 10% rate. Div. Ex. 1, p. 465. The REIT and stock market investments grow uninterrupted during a twelve-year period, ultimately leaving $1.4 million. Id., p. 465.

2. The Backtest Slides

a. The '73 Backtest

The slideshow reintroduces the Grizzly Bear Market following the three fictional investors and the Bucketeers. Id., p. 466. The following slide, titled "Back Tested Buckets," provides that the Bold Bucketeers' portfolio, with the same 40-20-40 investment assumptions, would be worth $1,544,789, twenty-one years after retiring on January 1, 1973 ('73 Backtest). Id., p. 467. The slide notes that the twenty-one year period compares to the same milestone at which the Balanced Buttafuccos had completely depleted their retirement portfolio. Id., p. 467. The dividend rate assumed for the REITs in the '73 Backtest is not disclosed in either the slideshow or the Webinar, although because the '73 Backtest contrasts what is essentially the Bold Bucketeers' portfolio against the same portfolio beginning on a particular date, it is likely to be 7.75% and seminar attendees would so assume. Div. Ex. 1, pp. 467-68; Div. Ex. 66, pp. 46-47. As with REIT returns, it is not entirely clear from the slideshow that the '73 Backtest assumed 3% inflation. Div. Ex. 1, p. 467. However, this fact does not appear to be in dispute. Resp. Br., p. 38.[11]

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[11] The "Back Tested Buckets" slide states that actual treasury rates of return were used for the bond bucket and S&P 500 returns were used for stocks. Id. Plum testified both that he did not know if that statement was true, and that it was false. Tr. 786, 874. Lucia testified that the actual S&P 500 Market rates for 1973 and 1974 were used, but that a flat 10% annual rate was used for each year thereafter. Tr. 1078-80. Lucia did not testify about the bond return used. Id. I find by a preponderance of the evidence that the statement was false, and that there is no evidence of the actual bond returns assumed. I note that Plum's

b. The '66 Backtest

Lucia next introduces backtests[12] for retirees who endure the market stagnation of the late 1960s.[13] Lucia introduced this section of his slideshow in 2005 or 2006. Tr. 1134-35. The first example, involving a 60/40 split of stocks and bonds (i.e., the Balanced Buttafuccos, although that name is not displayed in this portion of the slideshow), require $50,000 a year in inflation-indexed income. Div. Ex. 1, p. 472. The Buttafuccos' backtest, using actual S&P 500 returns for 1966-2003, actual United States Treasury Bill returns for 1966-2003, 3% inflation, and income from both stocks and bonds, are left with no income and a portfolio of just $30,000 by 2003.[14] Div. Ex. 1, p. 473.

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testimony on this point was very confusing. Plum initially testified that he did not know what bond returns were used, and that he believed that the same stock returns were used as for the Hendersons and the Buttafuccos. Tr. 786. However, the Hendersons' portfolio assumed both a 10% stock market return (in one scenario) and a return matching the S&P 500 (in the scenario beginning in January 1973), and the Buttafuccos' portfolio assumed a return matching the S&P 500, beginning in January 1973. Div. Ex. 1, pp. 427-28, 435.

[12] I use this term throughout the Findings of Fact only as a shorthand description of the contents of the slideshow. The meaning of the term, and its significance, is analyzed infra.

[13] The stock market between 1966 and 1982 produced stagnant returns. Tr. 1145-46, 1268. Lucia first began citing to the 1966 market stagnation period after consulting with his friend, actor and economic commentator Ben Stein. Div. Ex. 1, p. 470; Tr. 772. According to Lucia, the '66 Backtest was first conducted because of Stein's curiosity regarding BOM's results in a stagnant market. Tr. 1137-38.

[14] The Division's expert testified that the S&P 500 Market average is a commonly-used proxy for historical stock market returns. Tr. 944. Lucia and Plum testified that they used the S&P

Shifting back to the BOM strategy, the slideshow shows backtest results for the Buttafuccos, which again begins with $1 million in savings, requires $50,000 of inflation-indexed income per year, splits its investments 60% in stocks and 40% in bonds – no REITs – but with income from bonds first. Id., p. 474. Spending bond income first, according to the slide, allows the investors to collect $150,000 in income (presumably $50,000 indexed for inflation) in the year 2003, while maintaining a portfolio value of $1.2 million. Id., p. 475.

The next portfolio describes the BOM strategy, but with a 40-20-40 split with REITs (i.e., the Bold Bucketeers, although that name is not displayed in this portion of the slideshow). Id., pp. 476-77. The REITs are assumed to generate a 7% dividend rate. Id., p. 471. Unlike with the previous comparison of the four fictional investors, there was no explicit disclosure that the 7% REIT rate was hypothetical in the slides, nor was there an explanation for why the rate changed from 7.75%. Id., pp. 468-78.

With a pithy summary slide, Lucia declares, "[i]n 2003 . . . [a]fter adding REITs . . . [p]ortfolio value: $4.7 million[,] [a]nnual income: $150,000," more than tripling the portfolio balance. Div. Ex. 1, p. 477. Significantly, there are no fine-print disclaimers on any of the slides pertaining to the '66 Backtest, in contrast to virtually every other substantive slide, including those pertaining to the '73 Backtest. Div. Ex. 1, pp. 467-78.

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500 Market average as a proxy for historical stock market averages for the backtests. Tr. 794, 1284. Lucia and Plum also testified that United States Treasury Bill yields are reliable historical proxies for average bond rates, and that they used them as such in the backtests. Tr. 794, 1284.

E. Webinar

On February 16, 2009, Lucia broadcast a presentation (Webinar) over the internet. Div. Ex. 66, p. 1; Tr. 1244. Approximately the first two-thirds of the Webinar generally follows the same format and outline as the seminars, but does not use precisely the same slideshow.[15] For example, Lucia introduces a simplified version of the BOM strategy on pages 27-31 of the Webinar, earlier than in the seminar slideshow. Div. Ex. 1, pp. 410-12; Div. Ex. 66, pp. 27-31. The evidence is unclear as to why the Webinar deviates from the seminar slideshow. It may be that Lucia used a different slideshow in his internet presentations, or it may be that the slideshow changed between February 2009, when the Webinar aired, and 2010, when OCIE obtained a copy of the slideshow.

In any event, there are certain substantive differences between the Webinar and the 2010 slideshow. The Webinar sometimes calls non-traded REITs simply "real estate," and, if anything, the Webinar stresses the importance of REITs even more than does

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[15] For example, pages 364, 365, 367, 369, 370, 372, 373, 375, 378, 381, 384, 387, 390, 394, 406, 413, 416, 430, 438, 468, 469, 470, and 479 of the slideshow differ from the corresponding slides shown in the Webinar in certain non-substantive ways. Resp. Ex. 30; Div. Ex. 1. As another example, slides and hand drawings discussed on pages 13, 16, 17, 24-31, 34-38, 43, 47, and 56-58 of the Webinar do not appear in the slideshow, and pages 379, 389, 391, 415, 419, and 480-84 of the slideshow do not appear in the Webinar. Resp. Ex. 30; Div. Exs. 1, 66. Approximately the last third of the Webinar does not correspond to anything in the seminar slideshow. Div. Ex. 66, pp. 53-82. Oddly, the Webinar also states that Lucia only worked with salaried representatives. Div. Ex. 66, pp. 3, 51. In fact, the switch to purely salaried representatives occurred in 2011, well after the Webinar aired. Tr. 502, 1076-77, 1569.

the slideshow. Div. Ex. 66, pp. 34:12-14 ("we really focus a lot on nontradeable direct ownership in real estate"), 35:4-6 ("direct ownership in real estate . . . [is] not only a staple, it is critical"), 35:10-16 ("the Ibbotson data proves it, . . . a twenty percent addition to real estate investment trusts, be it tradeable or nontradeable, you end up with a higher rate of return at lower risk"), 44:19 ("real estate," in referring to the slide on page 449 of Div. Ex. 1, which states simply, "REIT"), 50:2-5 ("the real live [BOM] strategy . . . assume[s] we put . . . twenty percent in direct ownership in real estate," while displaying a slide showing "20% REITs"), 58:5-6, 19-20, 23-24 ("I'm going to put 300,000 dollars in my real estate bucket . . . the real estate can also help produce annuitized income . . . [and] will produce about 19,000 dollars per year"), and 69:17-18 ("the nontradeable real estate and all the safe buckets that we've talked about"). The first "Notes & Disclaimers (REITS)" slide in the slideshow does not appear in the Webinar at all, and although the second "Notes & Disclaimers (REITS)" slide appears in the Webinar, it does not disclose the fact that REITs have limited liquidity, in contrast to the corresponding slide in the slideshow. Div. Ex. 1, pp. 415, 447; Div. Ex. 66, pp. 35, 44. When discussing the BOM strategy in detail, Lucia states "in the sixties, you could have got about $15,000 per year income, dividends from that real estate investment." Div. Ex. 66, p. 44:22-25. Before discussing the effects of REITs in connection with the '66 Backtest, Lucia repeatedly uses the term "pretend" when introducing his assumptions. Div. Ex. 66, pp. 40, 48. However, when he discusses the effects of REITs, he does not use the term "pretend." Div. Ex. 66, p. 50:5. He then summarizes the result of the BOM strategy: "the real Buckets

portfolio, using real estate, 4.7 million dollars." Div. Ex. 66, p. 51:18-19.

F. Backtest Designs

Lucia testified that he did some of the work on the '73 and '66 Backtests used for the slideshow presentations, and that he "manually" calculated at least some of the results.[16] Tr. 1089, 1095. He also testified that he did not believe he had to produce any support for the backtests to the Commission during its examination, because he did not believe he had to maintain such records. Tr. 1094-95. Lucia and Plum testified that for the '73 Backtest, and for the fictional investors' results, Brian Johnson (Johnson) ran the calculations for the slides under Plum's supervision. Tr. 782-83, 839, 1088. Johnson was a junior employee who dated Lucia's daughter and, Lucia believed, had just graduated from United States International University, Lucia's alma mater, when he prepared the slides. Tr. 783, 1089. Plum did not check Johnson's calculations, but he reviewed his methodology and agreed it was correct. Tr. 784. Supporting documentation for the '73 Backtest calculations has never surfaced. Tr. 788.

In response to an investigative request for backtest slide support, Ochs produced two spreadsheets that she had received from Plum. Div. Exs. 12, 13; Tr. 87-89, 539-40.[17] The first spreadsheet laid out

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[16] Lucia also claimed to have backtested the BOM strategy to 1987, although he had no documentary evidence of this. Tr. 1094. There are no allegations of Lucia having presented the results of a 1987 backtest to the public.

[17] It is undisputed that the first spreadsheet, Div. Ex. 13, which Ochs apparently believed was support for the '73 Backtest, was produced during the examination. Tr. 87-88, 541-42. It is disputed whether the second spreadsheet, Div. Ex. 12, produced as

calculations for a fictional 40-20-40 portfolio beginning in 1973, but did not match any of the numbers from the slideshow. Div. Ex. 13; Tr. 788. The first spreadsheet does not support the '73 Backtest, nor was it intended to; instead, it is an "illustration starting in 1973 with the difference between a distribution from a pro rata portfolio of 60/40 stocks and bonds and spend safe money first over volatile money." Tr. 802.

The second spreadsheet, prepared by Plum at Lucia's direction, was intended as support for the '66 Backtest with REITs. Div. Ex. 12; Tr. 810. No support was provided for the '66 Backtest portfolio without REITs. Tr. 811.

In the second spreadsheet, REITs provided a flat 7% dividend return, were invested on day one, January 1, 1966, and were held for ten years, liquidating at the end of 1975. Div. Ex. 12; Tr. 218. The REIT principal remained constant at $200,000 through the ten year investment. Upon liquidation, the $200,000 was reinvested in the stock market, where the rest of the portfolio remained, growing at actual historical returns. Div. Ex. 12.

Both spreadsheets assumed a flat 3% annual inflation rate. Tr. 765; Div. Exs. 12, 13. The '73 Backtest presentation also stated that it utilized a flat 3% inflation rate. Div. Ex. 1, pp. 465, 467. Neither spreadsheet accounted for costs or fees associated with investments. Tr. 156, 1284; Div. Exs. 12, 13. In the second spreadsheet, after the first fourteen years

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support for the '66 Backtest, was produced during the examination or later. Tr. 112, 540-41, 810-11. As explained infra, neither spreadsheet actually supports the slideshow's claims. Accordingly, the probative value of the date of production of the spreadsheets is minimal, and I find that both were produced in the course of the 2010 examination.

the first two buckets, containing REITS and bond equivalents, were depleted. Div. Ex. 12. The balance remained allocated to a bucket of stocks, that is, the third bucket, from which income was withdrawn for the remainder of the backtests. Id.

G. REITs

In its simplest form, a REIT is a company that procures capital from investors by selling equity shares, uses the capital to purchase income-producing real estate assets, collects income, such as rent, from the assets, and then distributes the earnings back to investors. Div. Ex. 70, p. 10. REITs first became available to the investing public in the 1970s, but only became widely available in the 1990s. Tr. 774.

As applicable here, there are two general categories of REITS, traded and non-traded. Div. Ex. 70, p. 10; Tr. 1622. Traded REITs are traded on exchanges, are priced regularly, and are highly liquid. Tr. 166, 218, 1622. Non-traded REITs are inherently illiquid securities due to the lack of public market. Tr. 728, 1380. They are considered long-term investments, and Lucia and RJLC encouraged investors to consider them as such. Tr. 1297, 1621-23. Lucia and RJLC usually told clients to hold REITs between ten and fifteen years. Div. Ex. 1, p. 447; Tr. 1623. Non-traded REITs are designed to liquidate, merge, or be offered publicly at the end of their expected life cycles. Tr. 1370, 1392, 1623. Cycles are often between five and eight years. Tr. 1369, 1623.[18] Some non-traded REIT

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[18] Lucia, Jr. testified that the cycles typically lasted between seven and eight years, while Respondents' expert, Gannon, testified that the average cycles lasted between five and seven years. Tr. 1623, 1369-70.

issuers offer redemptions at certain predetermined intervals, offering investors cash to liquidate their shares. Tr. 1298-99. Redemptions, however, usually offer less than the original principal investment. Tr. 1299.[19] According to Lucia, Jr., non-traded REIT liquidity events do not have an established history, because "they haven't been around for more than a decade and a half or so." Tr. 1623.

As noted, non-traded REITs were the lifeblood of Lucia and RJLC's business, generating a substantial portion of revenues for them. Div. Ex. 4; Tr. 104, 1347. Additionally, non-traded REIT issuers offered the vast majority of marketing reimbursements to Lucia for hosting seminars and selling their products. Div. Exs. 4, pp. 5, 52; Tr. 104-05, 472, 483, 1077. Lucia himself was general partner or managing member of nine pooled-investment vehicles that invest in and manage real estate holdings. Div. Ex. 2, p. 9. Lucia and RJLC advocated, as an integral part of BOM, the use of real estate, specifically non-traded REITs, to prospective investors looking to "bucketize." Div. Ex. 1, pp. 471-78; Tr. 76, 1296-97; Div. Ex. 66, p. 35. Lucia cited reasons for advocating non-traded REITS as their relative lack of volatility and their ability to pay higher dividend rates than most traded REITS. Tr. 76, 1297, 1373.

H. Inflation

The Division alleges that Lucia's use of a flat 3% inflation rate for the backtest slides was materially misleading because the historical rates, which the Division alleges should have been used in backtests,

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[19] Lucia testified that many non-traded REITs have one-year redemption windows for repurchase of shares at about 90% of the original capital investment. Tr. 1299.

were significantly higher and would have negatively impacted the returns Respondents presented. Bryan Bennett (Bennett), an attorney adviser and former examiner in the Commission's Los Angeles regional office, testified that the Office of Compliance Inspections and Examinations (OCIE) recalculated what it believed was the '66 Backtest using inflation rates from the Consumer Price Index (CPI) maintained by the Bureau of Labor Statistics (BLS) and determined that the portfolio would have run out of money by 1986. Tr. 56-57, 81, 110-11. OCIE also calculated a 4.8% average inflation rate for the years 1966-2003 using CPI. Tr. 111. Bennett stated that BLS-gathered inflation rates are available online. Tr. 93.

Plum testified that Lucia made the decision to utilize a 3% flat rate for inflation in his backtests and that he had no problem with it. Tr. 776. Plum testified that he was aware that historical inflation rates were available, and he agreed that Bennett's calculation of a 4.8% average inflation rate for 1966 to 2003 was correct based upon BLS data, but stated that he did not believe the 4.8% rate accurately reflected inflation for retirees. Tr. 776-77. In his experience, Plum testified, retirees tend to spend less and have an inflation rate lower than CPI, thus, he believed 3% is a more accurate rate for retirees. Tr. 776-77, 867. Plum ran the '66 Backtest using the 4.8% average rate following institution of this proceeding, and agreed that the assumed portfolio would have run out of money earlier than 2003. Tr. 800, 815-16. Plum testified both that he did not know at the time of the '66 Backtest creation that historical inflation rates exceeded 3%, and that he knew "at times" that in the late 1970s and early 1980s, inflation had been double digits. Tr. 794-96. He testified that increasing inflation in the backtests would cause the backtests to run

out of money earlier, but qualified this by stating that BOM portfolios would still fare better than non-BOM portfolios. Tr. 800, 816. Although Plum testified he "ran" the '66 Backtest using inflation of 4.8%, no documentary evidence of such a test has surfaced. Tr. 800.

Lucia frequently stated that the BOM strategy would "provide inflation adjusted income for life" as a way of promoting use of the strategy. Tr. 1082-83. He assumed 3% inflation because it is a "generally accepted and reasonable" amount for forward-looking projections, which was what he says he was actually offering in his backtests. Tr. 1144-45, 1149. According to Lucia, he created the '66 Backtest in response to a question from Ben Stein, and Lucia presented it as a "forward-looking hypothetical" projecting a 3% rate. Tr. 1137-38. Lucia testified that the inflation rate in 1966 was 2.9% and that a 3% rate looking forward from that point was a reasonable projection. Tr. 1326. Lucia also stated that 3% was reasonable because the 100-year average of CPI is 3%. Tr. 1289. Lucia agreed that historical inflation data was publicly available, and he testified that he knew, intuitively, that historical inflation rates were higher than 3%. Tr. 1149, 1191. He testified that he understood that inflation rates were as high as double digits in the late 1970s and early 1980s. Tr. 1136.

Lucia testified that retirees spend less money than non-retirees and that inflation rates and cost of living increases for them are different than for non-retiree consumer spending. Tr. 1174-75. Lucia's position was based upon studies that he has researched and anecdotal experience with his 87-year old father. 1175-76. He cited to studies by various academics and

practitioners who concluded that inflation rates impact seniors differently than ordinary investors. Tr. 1289-90. Lucia did not dispute that using a higher inflation rate in the backtests would cause the assumed portfolios to run out of money sooner. Tr. 1150, 1203. Lucia added that the rest of the financial industry, including large investment houses like American Funds, used fixed assumed interest rates. Tr. 1147; Resp. Ex. 46.

The slideshow presented a 3% inflation rate for the Bucketeers' portfolio as "assumed" on only one slide; there is no similar disclosure elsewhere among the slides. Div. Ex. 1, pp. 422, 432, 465, 471-72, 474, 476. Lucia testified that he cautions seminar attendees that the 3% inflation rate is "assumed," or "pretend," and that actual historical rates were higher. Tr. 1190. Lucia stated in the Webinar, when staging the '66 Backtest with a 3% inflation rate, as evidence of his disclosures: "And let's pretend that from that point forward, inflation was 3 percent. We knew it was more. But we wouldn't have known that at the time." Tr. 1340; Resp. Ex. 30; Div. Ex. 66, pp. 48-49. Bennett agreed that the use of a 3% inflation rate was disclosed as an assumed rate on the slide for the non-backtested Bucketeers' portfolio. Tr. 135.

Lucia maintained during testimony that inflation rate projections often depend upon individual investor needs, which are discussed with potential clients when meeting with RJLC advisers and designing their individual BOM plans. Tr. 1143. This point was also made by Plum and Janean Stripe (Stripe), an RJLC adviser, in their testimony. Tr. 798, 1562.

I. Fees

OCIE discovered during its examination that the backtests did not include deductions for fees, even though RJLC told OCIE it charged advisory fees on products it managed, including stocks that would typically be included in a growth bucket. Tr. 154-55; Div. Exs. 12, 13. According to Bennett, Lucia's failure to include fee deductions in the backtests rendered them misleading. Tr. 154-55.

Lucia testified that he excluded fees from the backtests because he was using proxies for investments in his presentations, including the S&P 500 Index, which is not a purchasable product, as a proxy for the stock market, and T-Bills, which RJLC did not sell, as a proxy for the bond market. Tr. 1284; Div. Ex. 1, p. 416. According to Lucia, by excluding fees in a proxy-based portfolio, he was following financial planning industry practice, citing to an American Funds brochure as an example. Tr. 1270-71, 1284; Resp. Ex. 46. Bennett acknowledged on cross-examination that fees were also not deducted from the non-BOM hypothetical investor portfolios. Tr. 156.

Lucia testified that fees vary for individual investors and that for certain investors, like Richard DeSipio (DeSipio), an investor witness, there were no advisory fees associated with their portfolios because they were self-managed. Tr. 1285. Lucia testified that he made very clear to attendees at his presentations that fees were an important consideration and that potential investors should be sure to discuss them with an adviser. Tr. 1283. He testified that he stated at his presentations that even small differences in fees can make a big difference in return. Tr. 1199. His emphasis, however, was to inform attendees about the importance of BOM ahead of taxes and fee

sensitivity; he said, listing in order of importance, "Strategy first, taxation, fee sensitivity." Tr. 1283.

Stripe testified that there is no standard advisory fee charged to each client. Tr. 1564. If a portion of a plan is actively managed, there may be advisory fees associated with it. Tr. 1546. Stripe testified that the number of clients she has that pay advisory fees is low, somewhere around 25% in 2009 and 2010, which was consistent with the number of clients paying fees around the time of her testimony. Tr. 1546. Lucia, Jr. testified that advisers offered a broad spectrum of products, some commission-based and some fee-based. Tr. 1604. For example, RJLC recommends commission- and fee-based REITs. Tr. 1653. Lucia, Jr. testified that approximately 20% of the revenue for RJLC-affiliated companies comes from fees and the rest from trailing commissions on annuities and mutual funds, and first-year commissions from products that include mutual funds, REITs, and fixed annuities. Tr. 1656.

Potential clients who meet with RJLC advisers are provided with fee disclosures. Tr. 1285. Stripe, herself an RJLC adviser, confirmed that advisers discuss fees when potential clients meet with an adviser. Tr. 1564. Bennett agreed that RJLC disclosed fees to clients when they came in for a BOM consultation. Tr. 157.

J. Rebucketization

Bennett testified that Respondents failed to either follow the BOM strategy in the '66 Backtest or disclose that they did not, which made it misleading. Tr. 94, 96. He explained that, pursuant to the BOM strategy, after depleting the first and second buckets, an inves-

tor would withdraw portions of the third bucket to replenish the first and second buckets. Tr. 94, 96. In the '66 Backtest, however, Respondents depleted the first two buckets without ever replenishing them; instead, the entire portfolio was left in the stock market. Tr. 94, 96.

Plum testified that rebucketizing can be an important component of the BOM strategy, and that it should be done for most BOM implementers. Tr. 856. He testified that it was not required, though. Tr. 883. He agreed that in the '66 Backtest, there was no rebucketization following the depletion of the REIT portfolio, and that for the period between 1981 and 2003, 100% of the investments were in the stock market. Tr. 858. Plum testified that they deliberately did not rebucketize the '66 Backtest because they did not want to confuse people. Tr. 859. He elaborated that the point of the illustration was to show that spending safe money first, rather than using a pro rata distribution, was a superior strategy, and that was the only variable changed from the non-BOM strategy. Tr. 859-60. Plum testified further that there is no standard BOM formula and the decision to rebucketize is made on an individual basis. Tr. 883.

Lucia testified that he made a conscious decision not to rebucketize[20] the '66 Backtest because it would be misleading to do so. Tr. 1131, 1322. He explained that he was comparing BOM with no rebucketizing to a non-BOM strategy with no rebucketizing, and so rebucketizing the '66 Backtest would be a disingenuous comparison. Tr. 1130-31. Lucia acknowledged that he knew that during the periods the backtest portfolio

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[20] Lucia sometimes used the term "rebalance" instead of "rebucketize." E.g., Tr. 1130-31; Div. Ex. 66, p. 80.

was invested entirely in stocks, the stock market produced above average returns. Tr. 1145.

Lucia acknowledged that he did not provide "specific" disclosures of the investment allocations in the '66 Backtest following the depletion of the bond and REIT buckets. Div. Ex. 1, pp. 470-478; Tr. 1131. He testified that he makes it apparent in his presentations that the backtests are not rebucketized and provides context that would make the audience aware that the portfolio ends up invested completely in stocks, but explains that "in real life . . . it doesn't work that way." Tr. 1131, 1188-89. Lucia testified that though he did not include a slide indicating that the backtested portfolio ended up invested entirely in the stock market, he regularly engaged in an "oral conversation" with the audience and hand-drew illustrations explaining that rebalancing is not always necessary. Tr. 1186-87. He testified that he explained that academic research showed that stock investments have a 25-year time horizon, and investors can live off the dividends or income stream from the equity. Tr. 1186-87. He testified that academic research suggests that investors do not need to rebalance portfolios, and that he does not advocate it. Tr. 1132.

Plum and Lucia both acknowledged that the BOM strategy advocates against investing entirely in the stock market. Tr. 729-30, 1132, 1188. Ochs testified that Lucia has never advocated being invested 100% in the stock market, and that part of the BOM strategy involved replenishing the safe buckets when they are depleted. Tr. 536, 614.

Lucia testified that rebucketizing would be discussed on an individual basis by RJLC advisers with potential investors. Tr. 1130, 43. Lucia, Jr. and Stripe agreed. Tr. 1568, 1665. Lucia stated that he

always counsels attendees to meet with an adviser if they are interested in pursuing a BOM strategy, and to consider different scenarios before choosing a specific strategy. Tr. 1143, 1151, 1341.

K. Commission Examinations

In August 2003, compliance examiners from the Commission's Division of Investment Management's compliance office, a precursor office to OCIE, conducted an inspection of RJLC. Tr. 1478-79. That inspection uncovered several deficiencies, including inadequate disclosures of certain conflicts of interest and misleading statements about RJLC's business in its marketing materials. Div. Ex. 2, p. 7. These findings were reported to RJLC in a deficiency letter issued to the company on December 12, 2003. Resp. Ex. 13; Tr. 1492. One such deficiency pertained to a financial plan (not a slideshow) prepared for a client, in which RJLC made unsubstantiated and "highly unlikely" claims regarding REIT returns. Resp. Ex. 13, p. 6. The financial plan specifically mentioned that "income from the [REIT] could be used to supplement your Bucket #1 income." Id., p. 6 (emphasis omitted). RJLC told the 2003 examiners that it would correct the deficiencies. Resp. Ex. 14.

In March 2010, OCIE conducted an examination of RJLC and Lucia Financial, and OCIE found that RJLC had committed significant violations of the Advisers Act. Div. Exs. 2, 4. The examination was the impetus for the present enforcement action, and was triggered by a tip from the Division. Tr. 183, 185. OCIE issued a deficiency letter to RJLC on December 17, 2010, which outlined the deficiencies that form the basis of the present enforcement action. Div. Ex. 3; Tr. 70. Two of the noted deficiencies involved REITs, specifically that RJLC's marketing materials neither

(1) disclosed that non-traded REITs were not available during significant portions of the backtest period, nor (2) disclosed the illiquidity of non-traded REITs. Div. Ex. 2, p. 14; Div. Ex. 3, pp. 6-7. OCIE also found that RJLC had corrected some but not all deficiencies identified in the December 12, 2003, deficiency letter. Div. Ex. 2, p. 7.

As part of the examination, Bennett drafted an examination report. Resp. Ex. 50; Tr. 182. The report's cover letter, or "buckslip," was initially signed by three OCIE staff members on November 4, 2010. Resp. Ex. 50, p. 1; Tr. 29. The fourth and most senior staff member, Martin J. Murphy (Murphy), Associate Regional Director of the Los Angeles Regional Office, signed the buckslip on November 8, 2010. Resp. Ex. 50, p. 1; Tr. 181. After reviewing the report, Murphy had the matter referred to the Division because of the "seriousness of the advertising deficiencies." Tr. 184. The buckslip indicated no referral had been made to the Division; it is unclear why Murphy signed it first, and then initiated a referral. Resp. Ex. 50, p. 1. At some point, the examination staff met with the Division, and it was decided to amend the examination report by adding allegations of violations of Sections 206(1), 206(2), and 206(4) of the Advisers Act, and rules thereunder, and by noting on the buckslip that a Division referral had been made. Tr. 200; Resp. Ex. 51. No later than November 22, 2010, the Division decided to open an investigation. Resp. Ex. 53, p. 2. A formal order of investigation (FOI) was approved on December 2, 2010, and the final version of the examination report was signed on December 16, 2010. Resp. Exs. 12, 51. Respondents first learned of the existence of the FOI in May 2011. Resp. Ex. 12. No Division staff asked Bennett to obtain information for the Division through the examination process. Tr. 214.

L. Expert Testimony

a. REITs

Dr. Steven Grenadier (Grenadier) testified as an expert witness for the Division on all the various issues that it asserts made Respondents' slideshow presentations misleading. Grenadier's expert report concluded that Lucia's assumed REIT dividend rates for the backtests were misleading, creating inaccurate returns for the fictional investors. Div. Ex. 70, pp. 10-11. Grenadier based his findings on indices published by the National Association of Real Estate Investment Trusts (NAREIT), specifically the FTSE NAREIT All REIT index.[21] Div. Ex. 70, p. 10 n.24; Tr. 944. NAREIT indices are well-known proxies for REIT returns. Div. Ex. 70, p. 11; Tr. 944. Grenadier found that there were very few publicly traded REITs available in 1966, at the start of the 1966 backtest. Div. Ex. 70, pp. 11-12. He found that public non-traded REITs were relatively more available as of 1966, but were illiquid. Div. Ex. 70, p. 12. Additionally, NAREIT, the most famous REIT index, began reporting in 1972, six years after the '66 Backtest began using its assumed 7% return. Div. Ex. 70, p. 11; Tr. 944. He also found that using the NAREIT All REIT index provided significantly lower returns for the REIT principal and total portfolio for the '73 and '66

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[21] Grenadier testified that he used the All REIT index instead of specifying the equity REIT index because the All REIT index represents a general proxy average for the industry, much like why Lucia used the S&P 500 Market as a proxy for the stock market in general. Furthermore, Grenadier considered the All REIT index over the equity REIT index because the proportion of mortgage REITS might have been higher in the 1970s, which was when the bulk of the '66 Backtest REIT investment was supposed to have occurred. Tr. 962.

Backtests. Div. Ex. 70, p. 11 & n.24; Tr. 961-62. Grenadier also took issue with the assumption in the backtest that REITs could grow at a risk-free, flat rate, and then be easily liquidated. Div. Ex. 70, p. 12; Tr. 943.

Using actual historical data, Grenadier showed, lowered the REIT principal investment substantially. Div. Ex. 70, Ex. 5a. When the REIT investment ended in 1975 by liquidation, the backtest showed the REIT, with historical rates, at $85,646, not $200,000. Id.

Respondents called Kevin Gannon (Gannon) as an expert witness to testify on the issue of REITs as they were used in the '73 Backtest and '66 Backtest. Gannon's report concluded that the assumed REIT rates were reasonable. Resp. Ex. 34, p. 7; Tr. 1366. His report found that between 1972 and 2003, the internal rate of return was 12.9%, which was "so high that a 7% [rate] is clearly reasonable." Resp. Ex. 34, p. 4; Tr. 1390.

Gannon took issue with Grenadier's use of the NAREIT All REIT index. Tr. 1374-76. Gannon testified that the Equity REIT index, which includes REITs invested only in real estate equity, was the more reasonable index to consider. Tr. 1374. As part of his rationale, he found that the more widely used REIT index today is the Morgan Stanley REIT index, which is focused upon equity REITS. Tr. 1374, 1376. Gannon also concluded that equity REITs were the subject of the backtests because at least two slides in Lucia's slideshow cited statistics from the NAREIT Equity REIT index. Tr. 1374-75; Div. Ex. 1, p. 416.

Gannon's report recognized that REIT historical data was not available for the six-year period prior to 1972. Resp. Ex. 34, p. 6; Tr. 1366. He also admitted

on cross-examination that REITs were generally not available between 1966 and 1971 and that non-traded REITs are illiquid. Tr. 1378-80. To compensate for the unavailability of REITs from 1966 through 1971, Gannon created a model security based upon structured real estate investments during that period. Tr. 1380. The model was based upon inputs backed by thirteen assumptions. Tr. 1367, 1381. The model security produced a 7.1% internal rate of return. Resp. Ex. 34, p. 7; Tr. 1367. The evidence gathered for the model consisted of a single article, The Long Cycle in Real Estate, by Ronald W. Kaiser (Kaiser Article), which summarized total real estate returns between 1919 and 1995. Tr. 1378-79; Resp. Ex. 34, p. 7 & Ex. D (14 Journal of Real Estate Research, no. 3, 1997). The Kaiser Article drew its empirical data for the 1966-1971 period in part from a study published in 1976, How Real Estate Stacks Up to the S&P 500, by D. Kelleher in (Kelleher Study).[22] Resp. Ex. 34, p. 7 & Ex. D.

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[22] I find Gannon's testimony and expert report to be highly probative regarding the '66 Backtest. In addition to his significant concessions regarding REIT availability between 1966 and 1971 and REIT liquidity, both of which are specifically cited as deficiencies in the 2010 deficiency letter, a close examination of Gannon's supporting data is revealing. Div. Ex. 3, pp. 6-7. Gannon's report includes as Exhibit C a printout of the yearly NAREIT Equity REIT index averages. Resp. Ex. 34, Ex. C. Assuming without deciding that the NAREIT Equity REIT index was the appropriate data source, the price of an average REIT investment would have dropped substantially between 1972 and 1975, based on an index decline from 100 to 85.6. Id. Additionally, Gannon's starting assumption, that the "average total return" from real estate between 1966 and 1971 was 10.6%, was based on the Kelleher Study. Resp. Ex. 34, p. 7. The Kelleher Study, like the other studies cited in the Kaiser Article, and like Gannon himself, calculated "total return" or internal rate of return (IRR),

John S. Hekman, Ph.D (Hekman), the other expert witness for Respondents, could not recreate the '73 Backtest to achieve the same final portfolio figures presented in Lucia's slideshow. Tr. 1535-37. He testified that the term "backtest" was used on one slide in the slideshow, that the various examples in the slideshow were not, in his opinion, backtests, that his opinion was based on what an average investor would understand the term "backtest" to mean, and that the average investor would understand the term, in this context, to mean "using historical data to test a particular investment strategy."[23] Tr. 1402, 1423-26.

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i.e., the combination of dividends and price appreciation. Resp. Ex. 34, p. 3 & Ex. D, p. 237 n.4. Gannon ultimately estimates that the IRR between 1966 and 1971 for REITs would have been 7.1%. Id., p. 7. But Lucia did not tout the IRR for REITs, he touted the dividend rate. Div. Ex. 1, pp. 460, 465, 471. In other words, Gannon and Lucia were discussing two different returns: Gannon analyzed dividends plus price appreciation, and Lucia discussed just dividends. Gannon's evidence, therefore, does not really support Lucia's position; to the contrary, it undermines it. Specifically with respect to the '66 Backtest, Lucia assumed a 7% return, which represents the "annual," i.e. dividend, rate, and no price appreciation, according to the second spreadsheet. Div. Exs. 12, 1, p. 471. But Gannon concludes that, at least for 1966-71, the combination of yearly dividend and price appreciation is 7.1%. Resp. Ex. 34, p. 7. For the '66 Backtest to be consistent with Gannon's evidence, price appreciation would have to be approximately 0.1% between 1966 and 1971. This is, of course, highly unlikely, and it is much more likely that the price appreciation would have been higher, with a concomitant yearly dividend of less than 7%.

[23]. Hekman's testimony on these last two points is disjointed and confusing because he was repeatedly impeached on the subject, but I believe this to be a fair interpretation of what he said.

b. Inflation

Grenadier testified that a proper backtest, especially for a strategy that is supposedly able to keep up with inflation, should use historical inflation rates. Tr. 953, 978. Grenadier's expert report states that the results of the backtests were misleading because they did not use historical inflation rates; had they done so, both portfolios would have been completely drained by1986 for the '66 Backtest and 1989 for the '73 Backtest. Div. Ex. 70, pp. 6-8, Exs. 2a-3c. Grenadier determined the portfolios' collapse dates by using the same data used in Division Exhibits 12 and 13, but replacing the 3% inflation rate with actual historical inflation rates reported by BLS. Id., pp. 7-8, Ex. 2a-3c. Grenadier testified that the periods of the backtests included years of historically high inflation, including during the 1970s OPEC oil embargo. Tr. 941. Many of the high inflation years, according to Grenadier, occurred early in the backtest periods, which would have caused faster depletion of the portfolios because there would be smaller remaining investments to recoup losses. Tr. 941. Using an average inflation rate was, according to Grenadier, misleading, just as was use of an ahistorical rate. Div. Ex. 70, pp. 8-9. Grenadier admitted that the American Funds brochure Lucia discussed used an average 4% inflation rate in what the brochure called backtests, which he stated might be materially misleading. Tr. 974-76; Div. Ex. 46. Grenadier agreed that retirees over the age of 65 tend to spend less than their counterparts, but he testified that has nothing to do with inflation. Tr. 970-71. Grenadier also agreed that the rate of inflation between 1926 and 2003 averaged roughly 3%. Tr. 964-65.

Both Grenadier and Hekman testified that BLS publishes CPI for different categories of consumers. Tr. 937-38, 1527. CPI-U, for urban consumers, is the most commonly used measure of inflation. Tr. 937-38; Div. Ex. 70, pp. 7-8. CPI-E, which measures inflation for the elderly, is available for years after 1982. Div. Ex. 70, pp. 7-8. Grenadier tested the data in Div. Exs. 12 and 13 using CPI-U for the entire periods, which is reflected in Exhibits 2a, 2b, and 2c to his expert report, and he also tested the data using CPI-E, for periods after 1982, and CPI-U between 1966 and 1982, before CPI-E data became available, which is reflected in Exhibits 3a, 3b, and 3c to his expert report. Div. Ex. 70. In both sets of tests, the backtests ran out of money in 1986 and 1989 for '66 and '73, respectively. Id., pp. 7-8, Exs. 2a-3c. Grenadier testified that CPI-U and CPI-E differ year to year, but that CPI-E was higher than CPI-U during the relevant period. Tr. 940.

Hekman's expert report concluded that Respondents' use of a 3% inflation rate was reasonable. Resp. Ex. 35, pp. 1, 14; Tr. 1400-01. Hekman opined and testified that he considered Lucia's portfolio examples hypotheticals, not backtests, despite their being labeled as such, and that seminar attendees would understand as much. Tr. 1424, 1541-42; Resp. Ex. 35, pp. 3-4. He, thus, did not opine on the reasonableness of 3% as an inflation rate in a backtest. Tr. 1424, 1542; Resp. Ex. 35, pp. 3-4. Hekman opined that 3% is a commonly used hypothetical inflation rate, is used in many retirement and portfolio projections,[24] and is

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[24] Hekman cites to several large organizations that use a 3% inflation rate in their projections, including the U.S. Office of Personnel Management, TIAA-CREF, and CalPERS. Resp. Ex. 35, p. 5.

the historical average long-term rate for 1926 to the present. Resp. Ex. 35, pp. 4-5. As an added basis for his conclusion, Hekman opined that the inflation rate Lucia used did not affect the purpose of the investment hypothetical. Id., pp. 6-8. That is, the investment conclusion reasonable investors would draw from Lucia's hypothetical would have been the same whether or not Lucia used historical rates or the hypothetical 3% rate. Id., pp. 11-14.

Hekman opined that CPI is regarded as higher than true inflation, especially for seniors, citing a report from the Boskin Commission, created by the Senate Finance Committee in 1995 to study CPI (Boskin Report), and a paper by Professor Robert Gordon. Resp. Ex. 35, pp. 8-9; Tr. 1405. Hekman opined that a truer rate of inflation would incorporate a 1.2% reduction from CPI for the years between 1966 and 1996 and a 1% reduction beginning in 1997, as the Boskin Report suggests. Resp. Ex. 35, p. 9; Tr. 1405. After receiving Hekman's expert report, Grenadier ran the same tests using Hekman's proposed modified rate of inflation. Tr. 952, 967-68. Grenadier found that with the reduced inflation rates, the '66 backtest portfolio would have run out of money in 1993. Tr. 952. Hekman agreed that using his proposed reduced CPI rates would still cause the portfolio introduced as the '66 Backtest to run out of money in 1993. Resp. Ex. 35, Appx. 10; Tr. 1540.

Hekman further opined that seniors tend to spend less than average consumers and, thus, inflation would need to be corrected downward to reflect that fact. Resp. Ex. 35, pp. 13-14. Hekman determined that a 2% reduction each year from needed income would accurately reflect the true rate of inflation combined with seniors' reduced spending rates. Id., pp.

10, 13-14; Tr. 1539. Hekman testified that the 2% reduction was based upon studies by the Employee Benefits Research Institute (EBRI), which concluded that seniors tend to reduce their spending by about that much between the ages of 65 and 95. Tr. 1520. Inputting the reduced rate resulted in the '66 Backtest retaining $6.6 million in 2003. Resp. Ex. 35, pp. 13-14, Appx. 11.

c. Impact of Fees

Grenadier opined that the failure to include implementation costs and fees for the investments in the backtests produced significantly overstated and misleading results. Div. Ex. 70, pp. 2, 13-14. Grenadier opined that including implementation costs in a backtest is important because they may reduce or even eliminate the benefits of a strategy. Div. Ex. 70, p. 13. He wrote in his expert report that, at a minimum, funds that track the S&P 500, investments in T-Bills, and REIT investments would carry transaction and management costs. Id.; Tr. 945. It would be necessary, according to Grenadier, to incorporate actual or hypothetical costs into the backtests to provide a realistic result. Div. Ex. 70, pp. 13-14; Tr. 945. Accordingly, Grenadier incorporated example mutual fund fees, keeping all other data, including the 3% inflation rate that Lucia used, and found that both backtest results would be significantly reduced.[25] Div. Ex. 70, pp. 13-14; Tr. 945.

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[25] Grenadier noted in his expert report that there were generally no equity index funds that tracked the S&P 500 prior to 1977, so for between 1966 and 1976, he input average mutual fund fees for equity mutual funds, according to conservative estimates compiled by John C. Bogle in Bogle on Mutual Funds. Div. Ex. 70, p. 14. For after 1977, he used the rate collected by

Respondents did not offer any expert testimony on the issue of fees in the backtests.

d. Rebucketization

Grenadier's expert report states that a clear articulation and implementation of the strategy being tested is necessary to perform any backtest, as well as to verify the accuracy of any claimed backtest. Div. Ex. 70, p. 14. He found that Respondents' backtest illustrations did not present a clear asset allocation strategy, and the spreadsheets concentrate assets in a manner inconsistent with the BOM strategy as outlined in the rest of the presentation, making them improper backtests of the BOM strategy. Id., pp. 4, 14-15. Grenadier explained that the slideshow presentation discusses the importance of asset allocation, and that individual buckets are rebucketized periodically to maintain consistency in the strategy. Id., p. 15. According to Grenadier's expert report, the allocations presented in the slideshows for the '66 Backtest were not maintained over time, without explanation. Id. After the REIT and bond depletion, the '66 Backtest became entirely invested in the stock market. Id. Investment entirely in the stock market is inconsistent with discussions in the rest of the presentation urging asset allocation and diversification. Id., pp. 15-16. Grenadier included in his expert report graphs illustrating the benefit gained by Respondents by designing the backtest to allocate all investments into the stock market after depleting the first two buckets through withdrawals. Id., pp. Exs. 7a-7b. He testified that prior to the shift to the complete allocation into the stock market in the '66 Backtest, the market averaged 6% annual returns, whereas for the years after

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the Vanguard 500 Fund, which is one of the first equity index tracking funds and is considered one of the least expensive. Id.

1980, when the portfolio was entirely allocated to stocks, the market averaged 15% in annual returns. Tr. 948; Div. Ex. 70, Exs. 8a-8b. He concluded that failure to rebucketize the backtests, or failure to disclose that they were not, was misleading. Div. Ex. 70, pp. 14-17.

Respondents did not offer any expert testimony on the issue of rebucketizing.

M. Client Testimony

Two RJLC clients, DeSipio and Dennis Chisholm, testified at the hearing. Both were attendees at BOM presentations, DeSipio in Philadelphia, Pennsylvania, and Chisholm in Portland, Oregon. Tr. 247, 337. Chisholm also heard similar BOM discourse through Lucia's radio show, and read about the same, presumably in Lucia's books. Tr. 358-60. Both clients testified that the BOM presentations inspired them to meet with an RJLC advisor. Tr. 280-81, 370-71, 378-79. Both clients also invested in REITs because of what they learned at the presentations. Tr. 281, 283, 380.[26] A convincing aspect of the show, in particular, was the backtests.[27] Especially convincing to both clients was the effect of non-traded REITs. Tr. 266, 359-61, 368-69.

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[26] Q: Was it a large factor in your decision?

A [DeSipio]: Well, it was – it gave me – the whole purpose was – to me, I looked at it from the non-trade[d] REITs as another diversification which I was not aware of and did not have as far as financial asset allocation. Tr. 281.

[27] Chisholm testified, "If it was back-tested, I felt confident that somebody had done their homework and it proved somehow, some way, that this method was, indeed, a legitimate method of investing, of taking care of my retirement going forward." Tr. 362-63.

Both clients remembered Lucia presenting the backtests and using that term in conjunction with the '73 Backtest and '66 Backtest slides. Tr. 258, 359. Both clients understood the slides to suggest that Lucia used actual historical returns, or at least accurately reflected the approximate returns for the historical periods. Tr. 267-69, 371-72, 378. Both clients testified that they would have liked to have known that the backtests did not use historically accurate information. Tr. 288-91, 371-75. DeSipio did not recall being told that the inflation rate was assumed or hypothesized during the seminar, but recalled seeing a slide that said so. Tr. 295-96. He agreed that the slide summarizing the non-backtested Bucketeers' portfolio stated that it used an assumed rate. Tr. 295-96. Chisholm did not recall one way or the other whether Lucia said that the backtests used an assumed rate. Tr. 364. After being shown the same Bucketeers' slide as DeSipio, he agreed that it said it used an assumed 3% rate. Tr. 406. Both clients testified that they believed the 3% inflation rate used in the backtests was historically accurate or close thereto, and Chisholm testified he would have changed his opinion of the strategy if he had known the rate was not historically accurate and that historical rates would bankrupt the backtest portfolios. Tr. 260, 267, 364.

Both clients testified that they understood that for BOM to work, investors had to rebucketize. Tr. 250, 357. Chisholm testified that he was unaware that the backtests were not rebucketized, and he stated he would not have invested with RJLC had he known that fact. Tr. 374-75. Chisholm also testified that he did not remember Lucia disclosing that the backtests were not net of fees or the effect fees could have on the backtests. Tr. 374.

III. DISCUSSION AND ANALYSIS

A. Backtests

1. Definition

The parties dispute the definition of the term backtest. The Division asserts, through its expert, Grenadier, that, "[a] back-test of an investment strategy uses historical data to evaluate how that strategy would have actually performed had it been implemented in the past. Back-tests are generally conducted using actual, historical data – to the extent such data is available – especially for critical aspects of a particular investment strategy." Div. Ex. 70, p. 5. Grenadier bases his definition on "numerous textbooks and articles," discussing the importance of using actual, historical data. Id. Grenadier testified that he "very quickly" determined that the slideshow's presentation did not include proper backtests, according to the definition he offered. Tr. 960-61. Bennett, the OCIE examiner, testified that a backtest was a "method used to go backwards in time to see how a certain strategy would have performed using actual data points to calculate the performance." Tr. 114. Ochs had a similar understanding. Tr. 575. Bennett testified that what Lucia offered was not a proper backtest. Tr. 114.

Respondents' experts, Gannon and Hekman, both provided similar definitions of backtests – "Q: Is that because you would use actual data in a backtest? A [Gannon]: Yes;" "Q: [Y]ou agree that back-testing is generally understood as a process of evaluating a strategy, theory, or model by applying it to historical data? A [Hekman]: I understand – yes, I agree with that definition." Tr. 1387, 1421. Gannon testified that hypothetical rates of return should not be used in

backtests and Hekman testified that Lucia's analyses were not proper backtests. Tr. 1387, 1421.

Lucia disputes the backtest definitions given by the Division's expert, as well as by his own experts. Lucia testified that a backtest, "in the financial planning industry," was a "look back in history, but basing that on a forward-looking projection." Tr. 1093. Plum, too, claimed that he understood a backtest to mean a "hypothetical what if." Tr. 836. Lucia and Plum, the principal architects of the slideshow backtests, were the only two individuals who characterized the definition of backtests as something other than what the experts offered.

Lucia went on to state that this definition was based on what the financial planning industry "almost uniformly used." Tr. 1093. Despite Lucia's invocation of the "industry standard," none of the experts, including Respondents', corroborated that definition. Respondents also offered examples of backtests from several large investment houses, but those examples actually undermine Respondents' argument. Respondents point to Exhibit 46, a marketing pamphlet from American Funds, a large investment house, Exhibit 47, a marketing pamphlet from Fidelity Investments, and Exhibit 59, a marketing brochure from Financial Engines Income+, in support of what they assert is the industry usage of the term backtest. Tr. 1093; Resp. Br., p. 58. A review of Exhibit 46, however, reveals that actual "historical index returns" were used for the backtests, contradicting Respondents' assertion of what they proffer as the industry definition. Resp. Ex. 46. The example in Exhibit 47 used "historical monthly performance . . . represented by S&P 500, U.S. Intermediate –Term Government Bonds, and U.S. 30-day T-Bills." Resp. Ex. 47. Similarly, Exhibit

59, which does not specifically offer its models as backtests, uses only S&P 500 Market returns and Treasury Bond fund returns, both with factual, historical data. Resp. Ex. 59.

I also find that prospective investors would have understood the term in the same way as the experts. Dr. Hekman testified that the average investor would understand the term, in this context, to mean "using historical data to test a particular investment strategy." Tr. 1423-26. DeSipio understood the term to mean that actual performance data and actual inflation had been used. Tr. 267-69. Chisholm understood the term as a way of "prov[ing] somehow, some way, that this method was, indeed, a legitimate method of investing." Tr. 362-63.

I find the definition of "backtest" offered by all three experts the only consistent and intuitive one. Thus, a prospective investor at one of Lucia's seminars would have understood the term "backtest" to mean "using historical data to test a particular investment strategy."

2. Respondents' Use of Backtests

Lucia used the term backtest in his slideshow and narration, in his Webinar, in his training materials, and in his books. Div. Ex. 1, pp. 437, 467; Div. Ex. 50, p. 22; Div. Ex. 66, p. 47; Div. Ex. 68, p. 57. Lucia's employees, Ochs and Plum, and Lucia, Jr., testified that Lucia told audience members on numerous occasions at his seminars that he had "backtested" his strategy. Tr. 537, 880, 1686.

Notwithstanding Lucia's frequent invocation of the term backtest, the backtested slides used a jumble of actual historical returns and assumed returns. The slides for both backtests state that they used S&P

Market 500 averages and actual treasury rates of return. Div. Ex. 1, pp. 467, 471. Meanwhile, they used assumed dividend rates, including 7% for the '66 Backtest, probably a 7.75% dividend for the '73 Backtest, and a flat 3% inflation rate for both. Div. Ex. 1, pp. 467-78. It is quite clear that Lucia's backtest slides do not reflect properly conducted backtests.

Lucia, Lucia, Jr., and at least one senior employee of RJLC, after learning what the Division's definition of backtest was, tried to redefine what Respondents were providing with the backtest slides. Instead of a backtest, the slides represented: a "forward-looking hypothetical" (Lucia); "hypothetical forward-looking" scenarios (Plum); or "a simulation" (Lucia, Jr.). Tr. 1127, 840, 1627-29. Lucia also described what he was doing, at least for the '66 Backtest, as "pretending today is 1966." Tr. 1138. In the face of Lucia's persistent allusions to backtesting his strategy, I do not accept the inconsistent, after-the-fact descriptions of what Lucia and others testified Lucia was actually portraying, instead of a backtest.

3. Scope of the Backtests

The OIP alleges that "it was materially misleading for Respondents to claim that their alleged backtesting validated the BOM strategy," in connection with the 1966 and 1973 backtests. OIP, p. 7. In particular, the OIP alleges that "the BOM strategy," when backtested as presented in the slideshow, yields better outcomes than when backtested using actual historical data. Id., pp. 7-8. The OIP does not specifically allege that any claimed backtesting of the portfolios of the High Rolling Hendersons and the Balanced Buttafuccos, for comparative purposes, was

misleading. Div. Ex. 1, pp. 432 (discussing High Rolling Hendersons, assuming retirement on January 1, 1973), 437 (discussing Balanced Buttafuccos' results when "backtested to 1973-74" (footnote omitted)). The many slides devoted to the initial discussion of the Bold Bucketeers cover only 13 years, and it is not clear that either 1966 or 1973 is one of those years. Id., pp. 438-65. Indeed, the initial Bold Bucketeers discussion does not include any actual historical data, so it would not matter whether the discussion included 1966 or 1973; the outcome would be the same regardless of the period covered. Id., p. 465. It is only after the "'73/'74 Grizzly Bear" is introduced, and the assumptions become a mix of actual historical data and assumed data (for inflation and REIT returns), that the slideshow purports to compare the Bold Bucketeers with the Balanced Buttafuccos over a period including 1973. Id., pp. 466-68. Accordingly, although the OIP's citations to the "1973 backtest" could be construed as referring to purported backtesting both of the BOM strategy and of the portfolios of the High Rolling Hendersons and the Bold Bucketeers, it is more reasonable to construe it only as referring to purported backtesting of the BOM strategy starting in 1973 and 1966. Thus, although the entirety of the slideshow is relevant to this proceeding, I conclude that the focus of the OIP's allegations is on only thirteen pages of it. Div. Ex. 1, pp. 466-78.

B. The Central Importance of the Backtests

The backtest slides are the capstone of the slideshows, and the '66 Backtest is the pinnacle. Respondents imply that the backtests were discrete, standalone slides and meant little to the overall message. Resp. Br., p. 32. On that point, Respondents cite the fact that the word backtest was used only

twice in the entire slideshow. Resp. Br., p. 32. To the contrary, I find that the slideshow was a carefully orchestrated progression toward the backtests, which espoused the final proof that BOM, with REITs, is the best retirement strategy.

The first half of the slideshow is spent criticizing conventional investment wisdom and problems with following traditional portfolio models. It is only the second half of the presentation that begins the BOM strategy comparison. Lucia then uses a series of fictional investors who, following traditional investment advice, fail to obtain their retirement investment objectives. Div. Ex. 1, pp. 419-37. He makes certain assumptions for investment returns (actual returns for stocks and bonds and assumed returns for everything else) and inflation, runs the numbers, and presents the results. Id. He emphasizes that the High Rolling Hendersons and Balanced Buttafuccos suffer from the effects of the 1973 stock market, and ultimately characterizes his Balanced Buttafucco analysis as "backtested to 1973-74." Id., pp. 428, 435-37. He then analyzes the Bold Bucketeers using the same approach, but with a different asset allocation and withdrawal strategy than the previous fictional investors. Id., pp. 437-65. A reasonable prospective investor, viewing the slideshow's presentation of essentially the same methodology for the four different fictional investors, would understand that all four assumed portfolios had been backtested, just as the Balanced Buttafuccos' had.

The '73 Backtest slide, entitled "Back Tested Buckets," compares the Bold Bucketeers (who invest in REITs) to the Balanced Buttafuccos (who do not), over the period 1973 to 1994. Id., p. 467. The result is an investment principal in 1994 of $1,544,789 for

the Bold Bucketeers, compared to $0 for the Buttafuccos. Id., p. 467. The kicker comes, however, with the '66 Backtest. The '66 Backtest without REITs weathers thirty-eight years to provide an ending principal of $1.2 million. Id., p. 475. The next slides introduce the same investment portfolio, but add a 20% investment in REITs, and the ending principal of the portfolio more than triples to $4.7 million in the same period. Id., p. 478. To be sure, the slideshow does not explicitly display the term "backtest" in discussing the '66 Backtest. Id., pp. 468-78. However, it does use the term "Back Tested Buckets" in discussing the '73 Backtest, and in context the clear implication is that the 1966-2003 results were also backtested. Id., p. 467. For example, the slideshow asks, "what would have happened if you retired in 1966 . . .," and lists various "Notes and Assumptions," suggesting that the 1966-2003 results were analyzed in a way similar to the '73 Backtest. Div. Ex. 1, pp. 470-71. Any reasonable prospective investor would have interpreted these slides, too, as suggesting that the results had been backtested.

Respondents nonetheless argue that a reasonable investor would understand that the slideshows did not present backtests. Resp. Br., p. 17. Dr. Hekman testified that a reasonable investor would understand "that [the backtest slides] were not 'back-tests' of investment performance." Resp. Ex. 35, p. 14; Tr. 1433. But Dr. Hekman was not offered as an expert on how reasonable investors would understand a slide, nor is there any reason to privilege his opinion on this point over anyone else's. Additionally, Respondents argue that statements made by Lucia at slideshows, and some made during the Webinar, are proof that reasonable investors would understand that the backtests were just hypotheticals using hypothetical rates.

Resp. Br., p. 17. For example, Respondents cite to Lucia's statement, "we know it was more, but we wouldn't have known it at the time," regarding the 3% rate of inflation utilized during the Webinar. Div. Ex. 66, pp. 48-49. Lucia also used the term "pretend" multiple times in the Webinar, and the slideshow contains numerous disclaimers regarding "hypotheticals." Id., pp. 40, 48, 53; Div. Ex. 1, pp. 436, 448, 467. Respondents argue that such statements made it apparent that the backtests were hypotheticals with a forward-looking mentality. Resp. Br., p. 17; Resp. Reply, p. 22 n.29.

Nevertheless, the only two audience members to testify understood from the context that the backtests were presented as historically accurate. Tr. 267-69, 371-72, 377-78. No fine-print disclaimers appear on the slides discussing the '66 Backtest. Div. Ex. 1, pp. 472-78. In the Webinar, Lucia stopped using the term "pretend" after he started discussing the '66 Backtest. Div. Ex. 66, p. 50. The backtests use a mix of historical and ahistorical data, but the results are in every case presented as realistic enough to support substantial investments. Div. Ex. 1, pp. 467-78. Accordingly, I do not find Respondents' arguments regarding a reasonable investor's understanding of the backtests persuasive. That is, a reasonable investor would have understood that the '66 and '73 Backtests' data and assumptions were factual, historical, and realistic.

C. Importance of REITs in the Backtests

Even assuming that a reasonable investor would have understood that some data and assumptions were not realistic, the REIT assumptions are presented misleadingly. I conclude that a major focus of the backtests was to sell REITs, and the backtest slides' misleading statements on REITs were crucial

to Lucia's strategy. Respondents argue that the only purpose of the slideshow, and the backtests, was to demonstrate the effectiveness of the BOM strategy. Resp. Br., pp. 10-11. But selling REITs was at least an equally recognizable purpose. The progression from the "Buttafucco" portfolio to the "Bucketeer" portfolio, that is, from a portfolio that failed to one that succeeded, included only two new variables, BOM and REITs. Div. Ex. 1, pp. 437, 467. The only factor shown to audience members that differed between the backtest slide showing principal of $1.2 million and the following one, showing tripled principal of $4.7 million, was REITs. Div. Ex. 1, pp. 475-78.

Any doubt on this issue is dispelled by the Webinar.[28] In the Webinar, Lucia stresses that REITs, which he generally calls simply "real estate," are "critical" to the BOM strategy. Div. Ex. 66, pp. 34:12-14, 35:10-16. He states that REITs, both tradeable and nontradeable, provide "a higher rate of return at lower risk," which is the "holy grail of investing." Id., p. 35:14-16. He characterizes the "real live" BOM strategy as including twenty percent interest in real estate, while displaying a slide showing "20% REITs." Id., p.

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[28] Respondents place much emphasis on the Webinar, "urg[ing] this court to again review the Webinar prior to issuing a decision." Resp. Reply, p. 17. Respondents offered the Webinar because, they say, it is the only recordation of one of Lucia's slideshows. Resp. Br., pp. 16-17. The Webinar, according to Respondents, shows the full context of the slideshows with discussions that explain the slides that, viewed in a vacuum, are misconstrued. Resp. Br., pp. 16-17. As noted supra, there are numerous differences between the slideshow and the Webinar, some of them significant. Nonetheless, because consideration of the Webinar works almost entirely to Respondents' disadvantage, I accept their invitation to consider it "the best evidence of the BOM seminar presentation." Resp. Br., p. 16.

50:2-5. He emphasizes the value of "nontradeable" real estate, i.e., non-traded REITs. Id., p. 69:17-18. He compares a "pseudo [BOM] strategy," having no REITs, with "the real Buckets portfolio, using real estate, 4.7 million dollars." Id., p. 51:16-19. Plainly, the backtest slides' misleading statements on REITs were crucial to Lucia's strategy.

D. The REIT Rates and Usage were Unreasonable and Misleading

It is undisputed that neither the '66 nor the '73 Backtest meets the definition of "backtest" that I have adopted. Tr. 115-16, 960, 1402; Resp. Br., p. 32. But a prospective investor would have understood the slideshow as presenting the results of backtesting. Given these findings, the spreadsheets do not provide sufficient support for either the '66 or the '73 Backtest, or for the Webinar's version of those Backtests, and the slideshow itself did not provide sufficient transparency to prospective investors regarding either Backtest. More importantly, the various slideshow statements regarding REITs were misleading.

Based principally upon the expert testimony of Grenadier and Gannon, I find that Lucia's use of an assumed 7% dividend rate for the '66 Backtest and 7.75%[29] dividend rate for the '73 Backtest was misleading. First, the '66 Backtest invested in REITs on January 1, 1966, at a time when data on REITs were

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[29] As noted, it is unclear if this was the actual rate used because respondents produced no documentary support for the '73 Backtest numbers. However, the '73 Backtest slide contrasts the Bucketeers against the Buttafuccos, whose portfolio had an assumed 7.75% yearly dividend. Div. Ex. 1, pp. 465, 467. Accordingly, I conclude that a prospective investor attending one of Lucia's seminars would have understood the '73 Backtest to have assumed a 7.75% dividend rate.

unavailable, partly because there was no available index for REITs, but mainly because REITs themselves were largely unavailable. REIT data were unavailable until 1972, six years into the ten-year REIT investments in the '66 Backtest. There is no evidence that Lucia, Plum, or anyone else at RJLC did any sort of analysis like Gannon did for the period 1966-1971. Accordingly, the REIT returns for those years were essentially made up out of whole cloth. Furthermore, the rate that Gannon found with his model was based upon data from a single article, and was heavily burdened with subjective assumptions adopted solely by him. Tr. 1367, 1381. Additionally, as explained supra, even accepting Gannon's assumptions and model, his conclusion actually suggests that REIT dividends (as opposed to IRR) in 1966-1971, had there been any, would have been less than 7%.

Second, whichever index is used, the NAREIT All REIT or the NAREIT Equity REIT, it is clear that 1973 and 1974 produced significant losses for the REIT market as a whole. Div. Ex. 70, Ex. 5a (using NAREIT All REIT); Resp. Ex. 34, Exhibit C (showing NAREIT Equity REIT yearly returns for 1972-2003). Both the '66 Backtest and the '73 Backtest, because they began with REIT investments, would properly have shown substantial losses for any principal investment in 1973 and 1974. Using rates averaged through 2003 ignores the fact that the '66 Backtest invested in REITs in 1966 and held them for ten years, until 1975.[30] Div. Ex. 12. Thus, the principal invested in the stock market in 1975 following liquidation of

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[30] In context, it appears the REITs were purchased at the start of 1966 and sold at the end of 1975, a ten-year period. As noted, it is unclear how long the '73 Backtest held the REITs because no support was produced for it.

the REITs, should properly have been less than $200,000. Gannon's rationale that the dividend rates were reasonable for the period after 1972, because the average rate between 1972 and 2003 was 12.9%, ignores the fact that the REITs in the '66 Backtest were completely liquidated by 1975, leaving only a three-year sample, two of which were disastrous for REITs. Tr. at 1390; Div. Ex. 12.

Third, the '66 Backtest liquidated the REITs after an arbitrary ten years, despite the significant downturn in the real estate market in 1973 and 1974. Gannon testified that average REIT lifecycles last between five and seven years. Tr. 1370. True enough, a REIT could have a ten-year cycle, but according to Gannon's testimony, that would occur outside the norm. Tr. 1369-70. It was also convenient for Respondents to use a ten-year cycle. Liquidating anywhere within the five to seven year period would have exposed that principal to the Grizzly Bear Market for stocks – an asset which Lucia was actually calculating using historical returns. Instead, the ten-year period allowed Lucia to time the market perfectly, investing in the stock market as it rose again. Without liquidity events, there are few options to liquidate non-traded REITs, other than redemption for a discount to the principal investment. Tr. 1298-99, 1675. The assumed timing for the liquidity of the REITs in the '66 Backtest was, thus, unreasonable and its effect on the final number presented to prospective investors contributed to the backtest slide being misleading.

Fourth, the '66 Backtest as presented in the slideshow discloses neither the length of time REITs were assumed to have been held, nor whether the REIT principal remained constant. Div. Ex. 1, pp.

471-78. The Webinar was similarly silent on these assumptions. Div. Ex. 66, pp. 48-50. A prospective investor would not have known either how long the REITs were assumed to have been held, or the ending REIT principal amount.

Fifth, the Webinar is even more misleading than the slideshow. The first "Notes & Disclaimers (REITS)" slide in the slideshow does not appear in the Webinar at all, and although the second "Notes & Disclaimers (REITS)" slide appears in the Webinar, it does not disclose the fact that REITs have limited liquidity, in contrast to the corresponding slide in the slideshow. Div. Ex. 1, pp. 415, 447; Div. Ex. 66, pp. 35, 44. Before discussing the effects of REITs in connection with the '66 Backtest, Lucia repeatedly uses the term "pretend" when introducing his assumptions. Div. Ex. 66, pp. 40, 48. But when he discusses the effects of REITs, he does not use the term "pretend." Id., p. 50:5. When discussing the BOM strategy in detail, Lucia states "in the sixties, you could have got about $15,000 per year income, dividends from that real estate investment." Id., p. 44:22-25. This assumes a 7.5% dividend, which as noted supra, is false, and in context it is extremely misleading because it affirmatively avers that REITs were available for investment in the 1960's. Respondents' argument that the BOM strategy outperformed the comparative portfolios, "even assuming the actual historical rates were applied" to the '66 and '73 Backtests, is thus entirely unpersuasive. Resp. Br., p. 17.

E. The Inflation Rate Used was Unreasonable and Misleading

I find that Respondents' use of a 3% inflation rate, and failure to disclose that a historical rate would

have depleted the backtest portfolios after a short period, were misleading. A flat 3% rate was much lower than average rates during the times of the backtests, and such a downwardly-adjusted rate allowed the backtest portfolios to avoid running out of money far sooner than presented.

Grenadier testified that CPI-U is the "most common standard ubiquitous version of inflation data there is." Tr. 937-38. CPI-U, reported by BLS, indicates that historical inflation rates during the backtest periods were significantly higher than 3%. Div. Ex. 70, Exs. 2a-2c. During the late 1970s and early 1980s, CPI-U reached levels as high as 13.5%. Id. Seminar attendees were not advised that the inflation rate used was far below historical numbers and that use of even modified historical rates, accounting for biases, would have caused the backtest portfolios to drop to a zero balance years prior to 2003. OCIE calculated that the average inflation rate between 1966 and 2003 was 4.8%, much higher than the static 3% rate used in the backtests. Tr. 111. Grenadier verified that substituting historical CPI-U rates year by year into the backtests would cause the '66 Backtest to have a zero balance after 1986. Div. Ex. 70, pp. 8-9, Exs. 2a, 2c; Tr. 934-35. Annual CPI-E rates, which are readily available for 1982 through the present, and are purportedly reflective of inflation rates for elderly consumers, would also have resulted in the '66 Backtest going bankrupt in 1986. Div. Ex. 70, Ex. 3a.

Furthermore, as Grenadier noted, using a 3% average rate was misleading because the periods of higher inflation occurred early in the backtest periods, and use of historical rates would have rapidly reduced

principal balances. Tr. 941. Withdrawing significantly more income to keep up during the high inflation years would deplete assets much more quickly, and the remaining balances would have less room to grow, exacerbating losses. Tr. 941. None of these facts were disclosed to seminar attendees.

Respondents argue that CPI-U, and even CPI-E, are not reflective of inflation rates for retirees and elderly people because they tend to spend less as they age. Tr. 1175-77, 1290. Lucia bases his understanding of this concept in part on anecdotal evidence of his 87-year old father's diminished spending. Tr. 1186, 1291-92. This argument incorrectly conflates spending levels with inflation. CPI is determined, in essence, by comparing a basket of goods from a reference period to the fixed basket of goods at a measured time. Resp. Ex. 39, p. 5, Tr. 939. As Grenadier pointed out, the fact that people over the age of 65 tend to spend less "has nothing whatsoever to do with inflation." Tr. 971. As Grenadier went on to say, if Respondents wanted to reflect lower spending by retirees, they could have designed an example factoring in diminished consumption. Tr. 971. There is no evidence that Respondents marketed the BOM plan as one that survives retirement based upon the expectation that investors will spend less as they get older. Instead, they unequivocally presented the backtests as providing a steady inflation-adjusted income without regard to actual spending. Div. Ex. 1, pp. 422-24, 472; Resp. Ex. 30; Div. Ex. 66, pp. 11-12, 39. Additionally, as Grenadier testified, CPI-E was actually higher on average than CPI-U during the backtest period, which indicates that inflation levels for elderly consumers are

higher than for the non-elderly and weakens Respondents' argument that inflation rates are lower for elderly consumers. Tr. 940.[31]

Hekman's analysis, accounting for the fact that CPI-U purportedly overstated inflation by 1.2% (between 1966 and 1996) or 1% (from 1996 forward), provides little help to Respondents. Resp. Ex. 35, pp. 10. Even with these modified CPI-U rates, the '66 Backtest would have gone bankrupt after 1993. Resp. Ex. 35, Appx. 10. By 1980, when inflation peaked at 13.5%, Hekman's calculations, even with the 1.2% CPI-U haircut, left the portfolio with $916,388—more than $100,000 less than in the '66 Backtest. Div. Ex. 12; Resp. Ex. 35, Appx. 10. Regardless of how CPI-U was calibrated, there were years of very high inflation, and using 3% for those years was, by itself, unreasonable for the backtests.

Hekman engaged in a separate analysis factoring a 2% reduction in spending for retirees each year in addition to the 1.2% CPI-U haircut, which he based

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[31] Respondents claim that CPI-E is flawed because, among other things, it places significant weight on housing. Tr. 881-82, 1177, 1290-91. Hekman argues that the use of housing in the basket of goods is flawed because 80% of people over age 60 own their homes and 65% own them free and clear of a mortgage. Resp. Ex. 35, p. 10. It may be that CPI-E places too much emphasis on housing, but no evidence was submitted during the hearing to suggest that inflation rates, even for the elderly, averaged as low as 3% for the period between 1966 and 2003. Moreover, the 1995 release published by BLS on CPI-E, to which Hekman cited, explains that inflation had risen more rapidly for elderly that non-elderly consumers between 1990 and 1995, based upon a rise in prices among four of the seven largest spending categories in the consumption basket. Resp. Ex. 35, Attachment F. A major factor for this increase is the rapidly rising costs of medical care. Id. I am therefore not persuaded that the inflation rate for seniors is considerably lower than CPI-U.

upon cited studies. Resp. Ex. 35, Appx. 11; Tr. 1418. His analysis shaved an additional 2% off the 1.2% haircut to CPI-U he provided in his prior analysis, effectively providing a 3.2% decrease to CPI-U. Resp. Ex. 35, Appx. 11. This modification led (unrealistically) to negative inflation rates for certain years and a resulting balance of over $6.6 million in 2003. I do not find this argument particularly persuasive because, again, this was not what was presented to attendees, which is especially apparent due to the significantly higher ending balance than Respondents presented. Furthermore, even assuming a 3.2% decrease to CPI-U, the rate during the late 1970s and early 1980s would still have been much higher than 3%. For example, as Hekman's table provides, the rate in 1980 with these deductions was still 10.3%. Resp. Ex. 35, Appx. 11.

True enough, seminar attendees would understand that a flat 3% rate did not reflect year-by-year historical rates, especially because attendees were mostly retirees and near-retirees who lived through the tumultuous high-inflation years of the late 1970s and early 1980s, and would understand that inflation varies year to year. The attendees would have understood that the inflation rate for the early years of the backtests was not a static rate, but that use of a flat rate was intended to reflect an average. DeSipio testified that he was aware that the backtests used an average rate. Tr. 267. Furthermore, Lucia provided some context to the fact that the inflation rate did not track precise historical rates. For example, Lucia stated during the Webinar, regarding the inflation rate used for the '66 Backtest: "And let's pretend that from that point forward, inflation was 3 percent. We knew it was more. But we wouldn't have known that at the time." Resp. Ex. 30; Div. Ex. 66, pp. 48-49. This

single statement, assuming it was repeated regularly at seminars, let attendees know that the flat rate he used for the '66 Backtest was lower than historical inflation. Despite this limited disclosure that the rate used was not historically precise, seminar attendees did not know how far below historical numbers the 3% rate was. More importantly, they were never made aware of the crippling impact historical numbers would have on the backtests.

Whether it was appropriate to use an average rate or even an approximation in a backtest is not the crucial issue here. The fact that the '66 Backtest portfolio would have depleted its assets approximately 17 years before 2003, when it supposedly produced high balances, was misleading because Respondents, as Lucia admitted, regularly marketed the strategy as one that provides "inflation-adjusted income for life." Div. Ex. 8, p. 4; Tr. 741-42, 1082-83. Reasonable investors could not glean from the slideshow that the inflation rate used was completely disconnected from historical reality. Understanding that the inflation rates were completely ahistorical, and would bankrupt the backtest portfolios, would, as Chisholm testified, alter potential investors' confidence in the strategy. Tr. 364, 373. As Grenadier explained, the use of a fixed 3% inflation rate during the backtest period gave Respondents "the benefits of inflation but not the costs." Tr. 941.

Hekman provided evidence that many large financial institutions and the U.S. Government, among other entities, use a 3% inflation rate for retirement planning. He raises this point to argue that Respondents acted reasonably in using a 3% inflation rate. Resp. Ex. 35, pp. 4-5. I have no reason to doubt that

these institutions' projections are reasonable, as Hekman asserts. Indeed, courts are reluctant to admit expert testimony predicting future inflation, finding it an abuse of discretion. See, e.g., Taenzler v. Burlington Northern, 608 F.2d 796, 801 (8th Cir. 1979) ("Such testimony may present as an estimate a specific rate of future inflation more precise than present knowledge warrants."). Hekman's analysis in this regard misses the point, however, as he focuses upon what institutions project for future inflation levels. Hekman's and Respondents' argument in this regard hinges entirely on the assumption that the backtests were not backtests; rather, they were forward-looking projections. Lucia, as discussed, supra, did not offer projections. Instead, he offered carefully crafted backtests regarding performance of hypothetical BOM portfolios through historical periods.

Respondents argue that the BOM seminars were designed to show only that BOM would work better than the hypothetical investor portfolios that were compared to the backtests. Accordingly, Respondents argue, there was no performance advertising and the inflation rate was irrelevant as long as the methodology was consistent. Resp. Br., p. 43; Tr. 800. In fact, the methodology was not always consistent. As discussed, supra, the presentation introduced important variables into the backtests that were not used with the earlier hypothetical investors. The Balanced Buttafuccos maintained a simple 60/40 stock and bond portfolio, but the backtested Bucketeer portfolios included other items, most notably, REITs. Div. Ex. 1, p. 476; Resp. Ex. 30; Div. Ex. 66, p. 50. Additionally, the backtested portfolios migrated from pre-established return rates in the earlier hypotheticals, including the 10% assumed stock return rate and a 5.5% rate for bonds and CDs for the first Bold Bucketeer

hypothetical, to a historical stock return for the first two years and unknown bond returns in the '73 Backtest. Div. Ex. 1, p. 465; Resp. Ex. 30; Div. Ex. 66, p. 43. Most significantly, the '66 Backtest involved a stocks-only asset allocation beginning in 1980, when inflation peaked. Div. Ex. 12; Resp. Ex. 35, Appx. 10. Lucia stated in the Webinar that only "stock and/or real estate" would hold its value after taxes and inflation, which is why he recommended a "commitment to the stock market" to "manage the risk of inflation." Div. Ex. 30; Div. Ex. 66, pp. 11-12. But at no point does the Webinar (or the slideshow) disclose that that commitment in the '66 Backtest was total. Respondents' abandonment of the BOM strategy did not present a consistent methodology and artificially bolstered at least the '66 Backtest results. In essence, Respondents were comparing apples and oranges without disclosing that fact to seminar attendees.

Respondents point to brochures by American Funds, Fidelity, and Financial Engines Income+ as evidence of industry standards on backtests and use of averaged inflation rates in the backtests, which, they claim, shows that their use of a flat 3% rate was reasonable. Resp.. Exs. 46, 47, 59; Resp. Reply, p. 19-21. Their reliance on these brochures is misguided. The Fidelity brochure provides no insight into the exact inflation rates used, but makes clear that the withdrawal rates were inflation adjusted. Resp. Ex. 47. The Financial Engines Income+ brochure states, for what Respondents claim to be a backtest, that payout amounts rose on an annualized basis 2.4%. Resp. Ex. 59, p. 19. A close read, however, makes clear that annual payouts in its hypothetical portfolio increased by 254% from beginning to end, according to increases from investments, which it noted was a 61% increase after factoring in inflation. Id. 2.4% refers simply to

the average amount that payouts exceeded the inflation rate over twenty years. Id. American Funds' use of a 4% inflation rate, though an average, is still higher than the 3% Respondents used. Resp. Ex. 46.

F. Failure to Deduct Fees or Disclose Their Omission was Materially Misleading

The failure to take fees into account in the slideshow was misleading. As Grenadier wrote, "Implementation costs for a strategy are important because they may reduce, and at times eliminate, the benefits of a particular strategy." Div. Ex. 70, p. 13. That is certainly true of the backtested portfolios, and seminar attendees were unaware of how significantly the costs would eat away at the purported backtest results. Attendee witnesses DeSipio and Chisholm corroborated this fact. Tr. 289, 374.

The allusions to fees in the slideshow and in the Webinar are insufficient. Fees are discussed in only four areas in the slideshow: a generic legal disclaimer, general advice to try to keep fees low, general REIT disclaimers, and a footnote to a prepackaged Ibbotson slide used to tout diversification into real estate. See Div. Ex. 1, pp. 360, 415, 416, 447, 479. None of these pertain specifically to the backtests, and, in context, they are far too vague and general to constitute disclosure that fees were not deducted in the backtests. The only additional discussions of fees during the Webinar, which Lucia casts as representative of his full seminars, come during the explanation of mutual funds and in connection with an illustration of Lucia preparing a bucket portfolio on himself.[32] Resp. Ex.

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[32] It is worth noting that this discussion of mutual funds was part of Respondents' chastisement of a set of analysts' mutual fund buy and sell picks, which, Lucia says, would have lost

30; Div. Ex. 66, pp. 24, 62; see also Resp. Br., p. 16. Each is completely unconnected from the backtest discussions.

Respondents concede that advisory fees materially affect a portfolio's returns. Tr. 1199, 1203, 1285. Just as Respondents used proxies for the stock market and the bond market, using the S&P 500 and T-Bills, respectively, Respondents could have determined applicable fee proxies, much like Grenadier did in his expert report. See Div. Ex. 70, pp. 13-14, Exs. 6a-6b; Tr. 945. Respondents' argument that fees were difficult to predict because they were charged inconsistently, and sometimes not at all, is not credible. Tr. 1285, 1564, 1664-65; see also Resp. Reply, pp. 36-37. Respondents were surely acutely aware of the advisory fees, transaction costs, commissions, and management fees charged to clients. Tr. 1654-56, 1664-65. Respondents also received trailing commissions on certain products, including mutual funds. Tr. 1656. All of these fees, which produced a substantial portion of RJLC-affiliated companies' income, were tracked. Tr. 1656-57. Respondents had the capacity to estimate approximate fees for products that behaved like the S&P 500 index and conservative bonds, like they used in the backtests.

Respondents refer to the Fidelity, Financial Engines Income+, and American Funds brochures, which allegedly describe backtests similar to Respondents'. Resp. Reply, pp. 18-20; Resp. Exs. 46, 47, 59. These brochures do not help Respondents. The Financial

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money on the returns "minus .75%" – alluding to what I can only infer is a set of fees Respondents felt comfortable with as an average. Div. Ex. 66, p. 24. It seems Respondents are comfortable including fees when it helps illustrate their point, but not when it hurts it.

Engines Income+ brochure notes that estimated fees were included in the calculations, despite the fact that the portfolios included generic market-trending products, much like Respondents offer in the backtests. Resp. Ex. 59, p.18. This example severely weakens Respondents' argument that it would have been impossible and, indeed, misleading to include estimated fee levels. Fidelity did not include fees in their withdrawal rate hypothetical, but specifically disclosed that the backtested portfolio was not net of fees and that fees would significantly impact the portfolio. Resp. Ex. 47, p. 4. It is unclear whether the first chart in the American Funds brochure is net of fees. Resp. Ex. 46, p. 1. The second chart, using specific American Funds products, is specifically described as reflecting "net asset value." Resp. Ex. 46, p. 2.

The failure to take fees into account was also misleading because, as with inflation, the slideshow compared apples and oranges. Focusing just on the most pertinent thirteen pages of the slideshow, there are four scenarios: a first scenario (the '73 Backtest), in which the previously-described Bold Bucketeer portfolio (a 40-20-40 split between stocks, bonds, and REITs) is modified somewhat and then assumed to start in 1973 (Div. Ex. 1, pp. 466-68); a second scenario within the '66 Backtest, which assumed a 60-40 split between stocks and bonds and no use of the BOM strategy (Div. Ex. 1, pp. 469-73); a third scenario within the '66 Backtest, similar to the second scenario but using the BOM strategy (Div. Ex. 1, pp. 474-75); and a fourth scenario within the '66 Backtest, similar to the third scenario but with a 40-20-40 split between stocks, bonds, and REITs (Div. Ex. 1, p. 476-78). As noted, Div. Ex. 12 supports the calculation for the fourth scenario, but there is no support for the other

three, and Hekman could not recreate the slideshow's results for the first scenario. Tr. 802, 811, 1535-37.

Had these four scenarios been fairly comparable, the lack of fee disclosure might not have been misleading to prospective investors. For example, had all four scenarios maintained a 60-40 stock/bond split, had fees been some fixed percentage, and had the results been reported net of fees, the portfolio results would all presumably have been numerically lower, but the BOM strategy plus REITs may have performed better, all else equal, than not using BOM or not including REITs. But the four scenarios were not fairly comparable. Instead, two scenarios had REITs and two did not, at least two scenarios (the first and fourth) definitely did not rebucketize, one scenario (the fourth) ended up fully invested in stocks after 1980, and the third scenario may or may not have rebucketized. Resp. Br., p. 51. Because of the different asset allocations, both initially and over time, it cannot be assumed that fees would have been irrelevant. If fees are different for different assets, the overall fee load for the four scenarios will be different. It is a misleading oversimplification to assume, as Respondents essentially did, that the effect of fees is a wash.

Finally, Respondents argue that failure to include fees in the backtests is of no consequence because fees are fully disclosed when potential investors meet with an RJLC adviser. The Division does not allege that RJLC advisers failed to provide full disclosure concerning fees to potential investors, and I have no reason to doubt that they did. What is at issue, however, is whether it was misleading to fail to include fees or disclose their absence in the backtests. They did nei-

ther. After-the-fact disclosures, when potential investors meet with advisers, do not render the slideshow not misleading.

G. Failure to Disclose That the Backtests Were Not Rebucketized Was Misleading

The OIP alleges that Respondents "failed to reallocate assets after the bond and REIT buckets were exhausted" as to both backtests. OIP, p. 8. Failure by Respondents to disclose that the '66 Backtest portfolio (the fourth scenario, supra) remained completely invested in the stock market after the first fourteen years was misleading to seminar attendees. Although it is unclear from the slideshow whether there was or was not rebucketizing in the '73 Backtest, Respondents concede that there was no rebucketizing. Div. Ex. 1, p. 467; Resp. Br., p. 51. I find this failure to be misleading, as well.

The continuous message throughout the seminar presentation was that portfolios were structured to ensure there was always a safe bucket for withdrawals. This is evident both in the slideshow text, particularly the hypothetical investor illustration progression, and from the conversations that accompanied the slides, as shown by the Webinar. Respondents admit that they did not show any spreadsheets to seminar attendees to demonstrate where the buckets were allocated after the REITs and bonds were depleted. Tr. 1149. Nor did Lucia inform attendees, as part of the seminar, that the '66 Backtest portfolio was invested entirely in the stock market after 1980. Tr. 1131. Thus, seminar attendees did not have actual knowledge that the entire '66 Backtest portfolio was allocated to the stock market for over half of the portfolio lifespan.

The context of the slideshow suggested to seminar attendees that rebucketizing happened. The first BOM illustration for the Balanced Buttafuccos follows a twelve-year progression through which the investors withdrew income from buckets 1 and 2, representing safe and moderate-risk investments, plus the dividends from a REIT investment. Div. Ex. 1, pp. 448-461. Following those first twelve years, the first and second buckets are depleted, and the next slides show how the third-bucket assets, the REITs and a stock portfolio, grew from $562,000 to $1.4 million. Id., pp. 461-65. The conclusion on the "Buckets Overview" slide is that this $1.4 million bucket is available to "Re-Bucketize for another 12 years." Id., p. 465. The next set of slides, the '73 Backtest, purports to show that following a similar portfolio begun in 1973 would provide over $1.5 million after twenty-one years. Id., p. 467. Respondents concede there was no rebucketizing, but the slideshow suggests that Respondents followed the same methodology as before, that is, there was rebucketization. Lastly, the '66 Backtest portfolio purports to be a "Buckets of Money Portfolio," suggesting that it rebucketizes. Id., pp. 474-78.

Despite touting the power of the stock market generally, Lucia clearly advised attendees against exposing an entire portfolio to the stock market, which would lead reasonable investors to assume that Lucia would not leave a BOM portfolio completely in stocks. Lucia stated early in the Webinar, after extolling the general virtues of the stock market:

> So when you look at a slide like this, you've got to ask yourself, why wouldn't I put a hundred percent of my money into the stock mar-

> ket. And that's why [introducing slide illustrating high stock market volatility]. When you look at the volatility of the stock market, you see violent swings up and violent swings down. Don't need to explain to anybody about the violent swings down, because we certainly have experienced, what, a forty-percent decline in the last year.

Resp. Ex. 30; Div. Ex. 66, p. 7. Moreover, leading up to the introduction of the first BOM portfolio, the slideshow emphasizes the potentially disastrous possibilities of investing completely in the stock market. Lucia describes the High Rolling Hendersons, who invested completely in the stock market. Div. Ex. 1, pp. 427-432; Resp. Ex. 30; Div. Ex. 66, pp. 40-41. In one scenario, they received high returns. However, when the Hendersons begin their stock market investment in a bear market in 1973, the slideshow demonstrated that they go broke within seventeen years. Div. Ex. 1, p. 432; Resp. Ex. 30; Div. Ex. 66, p. 41. It recapitulates these poor results by discussing how stock market investments in 1973 took 12.8 years to equal the returns of T-Bills. Div. Ex. 1, pp. 429-31; Resp. Ex. 30; Div. Ex. 66, pp. 40-41.

Lucia testified that in addition to his oral discussions, he provided hand-drawn illustrations, which made clear to attendees how rebalancing would happen "in real life." Tr. 1187-89. There was nothing in the Webinar, however, to suggest that there was dialogue in the seminars to clue attendees into the fact that the '66 Backtest was not rebucketized, or that it was invested completely in the stock market for the majority of the backtest period. During the Webinar, Lucia made clear that the foundation of BOM was to

maintain diversity and to draw money from safe accounts over riskier accounts, emphasizing that there should be asset classes that do not "correlate positively all the time." Resp. Ex. 30; Div. Ex. 66, p. 34. Hearing BOM axioms like this, seminar attendees would not infer that the '66 Backtest left the entire portfolio in the stock market and drew income from it for fifteen to twenty years.

The Webinar is not helpful to Respondents on this point. Lucia said in the Webinar, "you never drain that stock portfolio for income." Resp. Ex. 30; Div. Ex. 66, p. 35. Lucia also quoted from an article by John J. Spitzer and Sandeep Singh titled, Is Rebalancing a Portfolio During Retirement Necessary? Tr. 1188; Resp. Ex. 37. He stated, "[w]ithdrawing the bonds first over stocks, performs the best . . . [t]his method, my little Buckets of Money method . . . also is most apt to leave a larger remaining balance at the end of thirty years." Resp. Ex. 30; Div. Ex. 66, p. 30 (internal quotations omitted). After the standard slideshow ended in the Webinar, he discussed additional hypotheticals, one of which assumed living off dividends from annuities and REITs, in addition to dividends from equity. Resp. Ex. 30; Div. Ex. 66, p. 66. A second hypothetical solves the problem of the stock market hypothetically imploding after fifteen years by taking REIT money that is still in the portfolio and replenishing the first two buckets. Resp. Ex. 30; Div. Ex. 66, p. 66-67. A third hypothetical posits that after fifteen years there is still money in the REIT bucket. Resp. Ex. 30; Div. Ex. 66, pp. 61-65. That seminar attendees "would have been informed at some point in the seminar that rebalancing wasn't necessary," is insufficient to render the backtests not misleading, because that infor-

mation was overwhelmed by the message that rebucketizing was part of a successful BOM strategy. Tr. 1188-89.

The attendee witnesses both testified that they understood BOM to require rebucketizing. Tr. 250, 357. DeSipio testified that he understood "[t]he whole idea was once you use your first bucket up, you took the . . . money from the second bucket and used that – poured that into the first bucket . . . then [when the second bucket was exhausted], you'd be using the third bucket to replenish the previous buckets going forward." Tr. 250. Chisholm testified that he understood that "it was imperative for [BOM] to work that you rebucketize . . .. It is what [BOM] was all about." Tr. 357. Chisholm went on to testify that he assumed the backtests were rebucketized because "that is what [BOM] is all about, to rebucketize, to reallocate, to draw down, to continuously replenish. I had no reason to believe he would not." Tr. 375. A reasonable investor would have been misled by the failure to rebucketize.

H. Misleading Impact of Historical Context

Respondents used the 1973 and 1966 retirement start dates in the slideshows to provoke sentiment in audience members who were predominantly retirees and near-retirees. These historical start dates were not arbitrary. Respondents assert that the Backtests were merely "forward-looking" hypotheticals to show BOM's efficacy. Resp. Br., p. 14. I disagree. To accept that argument discounts Respondents' calculated use of specific historical milieus. If Respondents' only goal was to demonstrate that BOM portfolios outlast conventional portfolios under any set of market conditions, start dates of 1973 and 1966 were not required,

nor would there be any reason to mix actual market with assumed market data.

The slideshow prefaces the backtests with historical context of the poor economic conditions plaguing the stock market from 1966 to 1982 and the acute problems in the market during 1973 and 1974. Div. Ex. 1. The presentation further primes the audience by representing how the non-bucketized – and non-REIT-invested – fictional investors would have fared, had they retired on January 1, 1966, and January 1, 1973. Id., pp. 471, 478. Many audience members who were retirees and pre-retirees would have lived through the market stagnation in the 1960s and the bear market in 1973-74. DeSipio understood the backtests to mean that the portfolios "held up under the various market conditions that occurred over the years." Tr. 268. Chisholm said, "It was my understanding that [the bear markets] would not be an issue because this was a proven method of investing, that it had been back-tested." Tr. 358.

I. The "Backtests" were not Merely "Hypotheticals"

Respondents argue that their use of the term backtest is scrutinized unfairly, and that what they offered were merely a series of "hypotheticals." Resp. Br., pp. 10-14, 32. Respondents support this argument by noting that the term "backtest" is only used twice in the slideshow; whereas, "hypothetical" is used thirty-seven times. Resp. Br., p. 32, n.38. Respondents also argue that, in hindsight, they would have used the term "hypothetical" instead. Resp. Br., p. 32. I do not find this convincing. Foremost, a backtest is, by definition, a realistic hypothetical. Tr. 115. Otherwise, there would be actual historical statistics for the actual portfolio. Similarly, the number of times

the terms are used does not diminish the emphasis on what the backtest slides represented: the grand culmination of the slideshow, hailing the triumph of the BOM portfolios, with REITs, over all of the fictional investors' portfolios. For the reasons discussed supra, the slideshow would be misleading even if the term backtest never appeared in it. The use of the term backtest by itself does not make the slideshow misleading – it only exacerbates it.

J. The Backtests were Misleadingly Offered as Scientific Findings

Respondents coated the backtest slideshows with the veneer of scientific methodology and due diligence. For example, Lucia stated during his Webinar that he told his friend Ben Stein, "You'd lose all respect for me if I hadn't done my homework. I have." Div. Ex. 66, p. 48. Lucia also began the Webinar by stating, "I'm going to show you the science behind retirement distribution planning, not really focusing on the art of speculation. There's a big difference between science – that which has been proven in finance labs all around the country – and art, which is, I don't know, pulling stuff out of the sky and trying to figure it out from there." Id., p. 4. Such language implies that Respondents applied proper diligence to prove that the strategy would endure the market conditions of the 1960s and 1970s. Despite what Lucia represented about backtesting to 1973 and 1966, he actually had insufficient support for the backtests. Even the minimal support produced by Plum includes arithmetical errors. Tr. 667, 1079-80; Div. Exs. 12, 13. RJLC had no procedures in place to determine whether calculations were accurate. Tr. 668. There is no evidence that anyone verified the numbers generated by Lucia's daughter's boyfriend, a recent college graduate.

Tr. 784. In sum, Lucia did, in fact, "pull[] stuff out of the sky." Div. Ex. 66, p. 4.

K. The Clients' Testimony Was Credible

Respondents argue that the testimony of the two RJLC clients, DeSipio and Chisholm, should be discounted. Resp. Br., pp. 52-54. DeSipio filed a Financial Industry Regulatory Authority (FINRA) arbitration claim which contained false allegations against Lucia, having to do with a mortgage-backed investment but not the BOM seminars. Tr. 318-19. He ultimately released Lucia from the case and admitted in writing that his claims against Lucia were false. Tr. 319. Because I sustained the Division's objection to four proposed exhibits pertaining to the FINRA claim, the precise nature of the claim and release are unclear. Tr. 309-12. In particular, there is no evidence that DeSipio's claim was verified, or that he made any knowingly false sworn statements in any filings in the FINRA case. Accordingly, the fact that his FINRA claim made false allegations reduces DeSipio's credibility somewhat; on the other hand, the fact that he released Lucia from the case and admitted that his claims against him were false, apparently without any consideration, restores his credibility somewhat. Overall, DeSipio's testimony was straightforward, with essentially no evasiveness, and his demeanor was sincere. I do not discredit any of his pertinent testimony.

Respondents also denigrate Chisholm's credibility based upon his failure to remember the precise order of when he attended BOM seminars and when he first met with an RJLC advisor. Resp. Br., p. 54 & n. 72. Chisholm initially testified that he invested with RJLC after seeing a BOM presentation in late 2009 or 2010. Tr. 434. However, Chisholm admitted during

cross-examination that he may have been influenced to invest through RJLC due to a show he attended in 2006, rather than the second one he attended in 2009 or 2010. Tr. 416. Or, alternatively, Chisholm was influenced to invest in REITs through RJLC based upon a combination of having seen the slideshow presentation, reading Lucia's books, and hearing his radio show. Tr. 336, 339, 1632. Admittedly, the holes in his memory would reduce his credibility if the timing of various events were crucial. But because Lucia offered the same backtest claims through all the media he used, I find it irrelevant whether Chisholm was mistaken about having contacted RJLC before or after the latest slideshow he attended. Even assuming that Chisholm became a client of RJLC after calling Lucia's radio show and asking to speak with a representative – as Lucia, Jr. testified, without any explanation for how he knew such facts – it is undisputed that Chisholm attended a BOM seminar prior to calling into the show. Tr. 1632. Respondents' argument that Chisholm became a client of RJLC "as a result of Lucia's radio show, not a BOM seminar" is not a reasonable inference from these facts. Resp. Br., p. 54, n. 72. Nor am I impressed by the fact that Chisholm has complained to multiple people about the REIT investment he made through RJLC, but not about the BOM seminar; to the contrary, that he complained to others actually bolsters his overall credibility, and that he complained only about his REIT investment actually supports the finding that Respondents had an overwhelming incentive to sell REITs, even to clients for whom they were not appropriate. As with DeSipio, I do not discredit any of Chisholm's pertinent testimony.

IV. CONCLUSIONS OF LAW

A. Sections 206(1) and 206(2) of the Advisers Act.

RJLC violated Sections 206(1) and 206(2) of the Advisers Act.[33] Section 206 provides:

> It shall be unlawful for any investment adviser, by use of the mails or any means or instrumentality of interstate commerce, directly or indirectly – (1) to employ any device, scheme, or artifice to defraud any client or prospective client; (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client.

15 U.S.C. § 80b-6. To establish violations under sections 206(1) and (2) of the Advisers Act, the Division must prove that RJLC was an investment adviser, that it engaged in fraudulent activities by jurisdictional means, and that it negligently breached its fiduciary duty by making false or misleading statements or omissions of material fact. SEC v. Merrill Scott & Assoc., Ltd., 505 F. Supp. 2d 1193 (D. Utah 2007); SEC v. Gotchey, No. 91-1855, 1992 WL 385284, *2 (4th Cir. Dec. 28, 1992); See SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 191-92 (1963). To establish a violation of Section 206(1), the Division

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[33] RJLC was the "maker" of the fraudulent statements under Janus Capital Group, Inc. v. First Derivative Traders, 131 S.Ct. 2296, 2302 (2011), because it "created" the materials and had ultimate legal control and responsibility for them. Tr. at 457. Lucia's statements and actions as the controlling and sole shareholder were offered as part of RJLC's marketing, and thus are imputed to RJLC.

must also prove that Lucia and RJLC acted with scienter. SEC v. Steadman, 967 F.2d 636, 641 & n.3 (D.C. Cir. 1992).

1. Registered Investment Advisers and Interstate Commerce

RJLC was a registered investment adviser from 2002 to 2011. RJLC Answer, p. 1. Lucia became a registered investment adviser in 1996 and, at least at the time of his Answer, was still a registered investment adviser. Lucia Answer, p. 2; Div. Ex. 2, p. 5. Lucia and RJLC engaged in interstate commerce. Lucia presented his slideshow to audience members and prospective investors across the country, visiting different cities around forty times a year. Tr. 1059, 1069-70. RJLC was a countrywide investment adviser, with at least fifteen offices in multiple states, including California, New Jersey, and Oregon. Tr. 280, 383, 1304.

2. Misrepresentations

Lucia and RJLC misrepresented the veracity of the backtests by using a misleading mix of historical and ahistorical information. The Division showed that Respondents provided misleading information about having backtested the information and that Respondents omitted material information about the assumptions used for the backtests.

Respondents misled prospective clients by portraying their conclusions as having been actually backtested and that the backtests used scientific methodology with realistic historical data and assumptions. Using that backdrop, Respondents misleadingly portrayed the '73 Backtest conclusion that, after twenty-one years, the fictional investors would maintain $1,544,789 in principal, as empirical proof of

the veracity of BOM with REITs. Nevertheless, Respondents were unable to provide any support for the '73 Backtest and their own expert could not recreate the '73 Backtest results.

Similarly, Respondents misleadingly presented to seminar audiences that they had backtested the BOM strategy to 1966, and that the BOM strategy, with the addition of REITs, culminated in a $4.7 million portfolio for the fictional investors. The spreadsheets offered as support in conjunction with actual historical data on REITs show that the conclusion offered in the slideshows was inaccurate and misleading because the REIT rate utilized was historically inaccurate and inflated, the REITs were invested at a time when they were unavailable, the REITs' liquidity was never impaired despite undisputed evidence that it would be, stable REIT investments were artificially assumed to have been made during the stock market drops in the early and mid-1970s, and the calculations were flawed and incorrect. The same is true of the backtests' use of a misleadingly low inflation rate, undisclosed exclusion of fees, and the failure to disclose that the backtests did not follow the BOM plan as advocated, which would have included rebucketizing and ensuring that the portfolios were not allocated completely to stocks.

Finally, the Commission is not required to prove reliance in an enforcement action and the lack of reliance is, therefore, not a defense. See e.g. SEC v. Simpson Capital Mgmt., Inc., 586 F. Supp. 2d 196, 201 (S.D.N.Y. 2008) ("Unlike private litigants, the SEC is not required to prove investor reliance . . . in an action for securities fraud."); SEC v. Rana Research, Inc., 8 F.3d 1358, 1363 & n.4 (9th Cir.1993); SEC v. Blavin, 760 F.2d 706, 711 (6th Cir.1985).

3. Scienter

Scienter is defined as a "mental state embracing the intent to deceive, manipulate, or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976); Aaron v. SEC, 446 U.S. 680, 686 n.5 (1980). A finding of recklessness satisfies the scienter requirement. David Disner, 52 S.E.C. 1217, 1222 & n.20 (1997); Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1568-9 (9th Cir. 1990), cert. denied, 499 U.S. 976 (1991) (citing eleven circuits holding that recklessness satisfies scienter in Section 10(b) and Rule 10b-5 actions). Recklessness, in the context of securities fraud, is "highly unreasonable" conduct, "which represents 'an extreme departure from the standards of ordinary care . . . to the extent that the danger was either known to the defendant or so obvious that the defendant must have been aware of it.'" Rolf v. Blyth, Eastman Dillon & Co., 570 F.2d 38, 47 (2d Cir. 1977) (quoting Sanders v. John Nuveen & Co., 554 F.2d 790, 793 (7th Cir. 1978)); see also S.W. Hatfield, CPA, Exchange Act Release No. 69930 (Jul. 3, 2013), 2013 WL 3339647 at *21.

The standard of care for a registered investment adviser is based on its fiduciary duty. See Transamerica Mortg. Adviser, Inc. v. Lewis, 444 U.S. 11, 17 (1979); Capital Gains Research Bureau 375 U.S. at 191-92. Investment advisers have an "affirmative duty of 'utmost good faith, and full and fair disclosure of all material facts.'" Capital Gains Research Bureau, 375 U.S. at 194 (citations omitted); Blavin, 760 F.2d at 711-12. Respondents were required to "employ reasonable care to avoid misleading" clients. See Capital Gains Research Bureau, 375 U.S. at 194; SEC v. Moran, 922 F. Supp. 867, 895-96 (S.D.N.Y. 1996). Ultimately, the standard is one of "reasonable

prudence, whether it usually is complied with or not." Vernazza v. SEC, 327 F.3d 851, 861 (9th Cir. 2003) (citation omitted). As applicable here, an investment adviser has a "professional duty to investigate the information upon which his recommendations [are] based" and to inform investors of risks. Blavin, 760 F.2d at 712; see SEC v. Fife, 311 F.3d 1, 10 (1stt Cir. 2002).

Lucia authored the slideshows and maintained ultimate control over them. Tr. 568, 1691. Lucia also engineered the backtests. Tr. 568, 776, 791-92, 1130, 1191. In doing so, Lucia deliberately chose to present: the backtest slides and language; the historical contexts of the backtests; the misleading REIT rate of 7% for the '66 Backtest; the span of years of the backtests, which shielded the REIT investments from stock market volatility; and for the '66 Backtest, an initial investment date of 1966, five years before most REITs were available, and before any published rates were available.[34] Lucia had full control over, was fully aware of, and actually committed the violations in this case, and Lucia's scienter is imputable to RJLC.

Respondents acted with the intent to deceive. Lucia agreed that if actual inflation was used in the '66 and '73 Backtests, the portfolios would have been depleted more quickly, and would have been "damaging" to the '66 Backtest. Tr. 1150-51, 1192:9. Lucia knew that disclosing that the BOM strategy would go bankrupt would not be helpful in attracting clients. Tr. 1151-52. An encounter between Bennett and Plum also supports a finding of intent, at least as to RJLC.

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[34] Respondents argued that the '66 Backtests were created only for the benefit of Ben Stein. Tr. 772, 1137. Even if the '66 Backtest was originally created for Stein's benefit, Lucia chose to add that backtest to his slideshow. Tr. 1191.

During the 2010 examination, Bennett asked Plum about the '66 and '73 Backtests; in particular, he pointed out that use of actual inflation rates rather than an assumed inflation rate resulted in depletion of assets. Tr. 91. Plum replied that "of course, [the BOM strategy] would have gone broke, but all the portfolios would have gone broke." Id. Plum, who attended a number of seminars with Lucia, thus knew that the backtests were unrealistic and that the slideshow presented misleading results. Tr. 734-36.

Lucia offered inconsistent and contradictory testimony as to why Respondents chose 3% for an inflation rate. Lucia at one point testified that 3% was a reasonable rate because it is what is commonly used in the industry in backtests. Tr. 1147-49. He also testified that he chose 3% because the inflation rate in 1966 was 2.9% and that it was reasonable to project that the rate would stay around 3% going forward. Tr. 1325-26. It is clear, however, that Lucia was not aware that the inflation rate in 1966 was near 2.9% when he designed the backtests. He testified, "I learned yesterday, incidentally, from Dr. Grenadier that the inflation rate in 1966 was, I believe I saw on the screen, 2.9 percent." Tr. 1267. Additionally, this reasoning would not explain why Lucia chose 3% as the projection rate in his '73 Backtest. Grenadier reported that CPI-U was 6.2% in 1973 and Hekman, according to his argued reduction of 1.2% from CPI-U, opined that a reasonably adjusted inflation rate in 1973 was 5%. Div. Ex. 70, p. Appx. 2a; Resp. Ex. 35, p. Appx. 10. Furthermore, the 2.9% rate for 1966 was measured by CPI-U, which Respondents repeatedly argued is a biasedly high rate. Further contradicting his own testimony, Lucia said that he actually did use CPI-U, but used the "average of what the CPI-U has been for the past hundred years." Tr. 1289; 1328-29.

Respondents were aware of the impact of fees on any investment and deliberately chose not to include fees or disclose that the totals at the end of the backtests were not net of fees, demonstrating an intent to keep attendees in the dark. During cross-examination, Lucia agreed that a managed portfolio that charges a fee and that produces the identical return of a non-managed portfolio would produce significantly less over a thirty to forty-year period. Tr. 1203. Lucia also testified that he could not have included fees in his backtests because they included products that RJLC did not manage. Tr. 1284. Specifically, he said, "if I show it charging a fee, I'm in trouble." Tr. 1284. That testimony is contradicted by the self-bucketing example that he provides during his slideshows and the relevant discussion in the Webinar. During the Webinar, he states, regarding a portfolio of hypothetical low-risk investment interests: "And if it lost two percent per year – let's say it grew at six percent in some diversified portfolio, but after fees, it only netted four percent, and you took out six, that's a minus two." Resp. Ex. 30; Div. Ex. 66, p. 62. Similarly, Lucia was willing to include estimates of a fee in his discussion of how they would drain a typical mutual fund portfolio. Resp. Ex. 30; Div. Ex. 66, p. 24. It is clear Lucia was willing to discuss hypothetical fees when it suited his message. His suggestion otherwise demonstrates an intent to purposefully exclude the fees to strengthen the returns of the backtests.

Respondents admitted that they deliberately chose not to rebucketize the backtests and to leave the entire balance in the stock market, and admitted they did not explicitly disclose either fact. Tr. 859, 1130, 1188-89. Their supposed reasoning for leaving the balance in stocks for the majority of the backtests'

lifespan was to ensure that they did not "cherry pick" the time to rebalance. Tr. 859, 1323, 1327. This is not plausible. Respondents acknowledged that they advocate against being invested completely in the stock market, but Lucia knew that the stock market produced above-average returns during the years that the backtest portfolios were allocated entirely to stocks. Tr. 536, 729-30, 1130, 1145. By structuring the backtest the way that they did, they took advantage of a higher-producing strategy, essentially engaging in cherry picking, than if they had rebucketized, the way attendees would have expected. The decision not to rebucketize, knowing (with hindsight) that the stock market produced impressive returns during the relevant period, demonstrates an intent to mislead.

Lucia discussed how Ben Stein was skeptical of the BOM strategy. Div. Ex. 66, p. 47. Lucia, however, satisfied Stein with what he asserted was a backtest. He stated: "Well, I did a backtest for Ben [Stein]." Id.; Tr. 1318. Lucia was clearly not telling Stein that he created a true hypothetical like with his fictional investors; rather he was claiming to use an actual backtest to prove that BOM worked, and he then did the same with seminar attendees. Similarly, he touted the BOM strategy as a "time-tested" one based upon "empirical evidence" and "science, not art." Div. Exs. 10, 16; Tr. 624-25, 1050, 1111. Lucia knew that the BOM strategy had not been backtested, as seminar attendees would have understood that term, as opposed to how the "financial industry" allegedly would have understood the term. This is demonstrated by the fact that what are called backtests in the slideshow do not qualify as either backtests or hypotheticals even under Lucia's definition. Lucia testified that a backtest is "forward-looking," even though

at least the '66 Backtest was a mix of historical and assumed data. Tr. 1127.

The misstatements on the "Back Tested Buckets" slide, although not charged in the OIP, also demonstrate an intent to deceive. Div. Ex. 1, p. 467. Plum's testimony and demeanor when questioned about the claimed use of treasury returns and S&P 500 returns suggest that he was, initially, sincerely confused about that slide. Lucia, by contrast, testified that he knew that the stock returns were not completely accurate and said nothing about the accuracy of the bond retrurns, and further testified that the inaccuracy was only discovered "within the last couple weeks." Tr. 1078-80. I find Lucia's testimony about the alleged discovery of the misstatements to be knowingly false. First, if he had truly discovered the problem weeks before his testimony, there is no reason he would not have told Plum, but Plum clearly knew nothing about it at the hearing. Second, it is utterly implausible that Lucia, who determined the contents of the slideshow and gave every seminar (in contrast to Plum, who did not attend them all), and has given them hundreds of times, would not be aware of the false information contained in the "Back Tested Buckets" slide. I conclude that Lucia knew of the misstatements and kept them in the slide to deceive prospective customers.

In some instances, Respondents acted recklessly. Lucia departed from the standards of care by not ensuring the accuracy of the information on which his recommendations were based, and this departure was extreme. The backtests were not supported by the spreadsheets or any other documentation, and Lucia testified that he did not think he was required to maintain such documentation. Allegedly, some

backtest calculations were generated by a junior analyst who was a recent college graduate and who apparently got his job because he was dating Lucia's daughter. Lucia's employees, particularly Ochs, apparently thought that the backtests were properly documented, because they produced documents that they believed constituted support for them, but were not, in fact, support. The inaccuracies discovered in the slideshow demonstrate that Lucia placed little emphasis on accuracy in the calculations he so enthusiastically presented to prospective investors. He also had no mechanism in place to correct inaccuracies. Tr. 667-68. Respondents contested the findings of the 2010 examination, and posted a video refutation of the OIP, before conducting the internal investigation which supposedly revealed errors in the '73 Backtest slides and the first spreadsheet. Tr. 1205-08. Lucia told Dr. Hekman that a mathematical error had been identified in the "Back Tested Buckets" slide. Tr. 1537-38; Div. Ex. 1, p. 467. However, Lucia testified disingenuously, as if he did not know of the error. Tr. 1080-81. It was not reasonably prudent, and it was an extreme departure from the standards of ordinary care, for the extensive number-crunching required to support the crucial parts of the slideshow, including the claims regarding the '66 and '73 Backtests, to be undocumented and irreproducible even by Respondents' own expert witness.

Lucia also departed from the standards of care in an extreme way by failing to inform seminar attendees of the risks of investing in REITs. Lucia failed to put in disclaimers in the '66 Backtest slides, from which a reasonable investor would have understood that the '66 Backtest slides were less "hypothetical" than the preceding slides. Div. Ex. 1, pp. 471-78. Although not so much a risk as an extremely material

fact, he also failed to inform seminar attendees that REITs were essentially unavailable prior to 1972, and that the spreadsheet allegedly supportive of the '66 Backtest assumed an investment in REITs spanning a bear market in stocks.

Given Lucia's extensive experience promoting REITs and long career as an investment adviser, and the large revenues he earned by selling them, he must have known that they were illiquid and essentially unavailable until 1971. Lucia nonetheless presented REITs, falsely and misleadingly, as if they were liquid and purchasable in 1966. When discussing the BOM strategy in detail during the Webinar, Lucia states "in the sixties, you could have got about $15,000 per year income, dividends from that real estate investment." Div. Ex. 66, p. 44:22-25. In the slideshow, REITs are allegedly backtested to 1966, and according to the spreadsheet, they are liquidated, conveniently, exactly when they are needed to refill the "safe" bucket. Div. Ex. 1, p. 478; Div. Ex. 12.

Respondents had a motive to misrepresent the facts about REITs: their non-traded REIT revenues were so significant to their bottom line that they had an overwhelming incentive to promote them. Lucia asserts now, and testified, that the BOM strategy is purely a "withdrawal" strategy, and is not an asset allocation strategy. Lucia's assertion is knowingly false. The backtest discussion in the slideshow is not merely a discussion of a withdrawal strategy, it is transparently a discussion of the benefits of investing in REITs, with the intent to lure prospective investors into buying them.

a. Lack of Investor Complaints

Respondents dispute the claim that they knew that the information they provided was misleading because, they argue, no audience members ever complained that such information was misleading. Resp. Br., p. 52-54. I do not find this argument convincing. It is not the responsibility of investors or prospective investors to make a respondent aware that something is misleading, it is the responsibility of advisors to act as their clients' and prospective clients' fiduciaries. Respondents cite no law in support of their argument, and indeed, Section 206 of the Advisers Act focuses upon the investment adviser and his or her actions. Clients and prospective clients are mentioned only in relation to the advisors. See SEC v. Gruss, 859 F. Supp. 2d 653, 662-63 (S.D.N.Y. 2012).

b. Reliance on Compliance Network and the Commission

Respondents argue that they could not have acted with scienter because multiple layers of internal and external compliance review vetted the materials, and none of them informed Lucia that the backtests were misleading. Resp. Br., p. 4, 54-56; Tr. 1607. In addition to its own compliance networks, Respondents argue that OCIE reviewed similar materials, including an earlier version of the slideshow, in 2003, and found no fault with it, essentially sanctioning the content. Resp. Br., p. 56. Respondents cite to SEC v. Slocum, Gordon & Co., 334 F. Supp. 2d 144 (D.R.I. 2004), in which the court found that the defendant relied upon independent external auditors and the Commission, neither of which raised issue with the defendant's account structure. I do not find merit in these arguments.

Respondents point to reviews by its network affiliated broker-dealers, first, Securities America, and second, First Allied, both of which cleared the slides, as wholesale endorsement of the backtests. Resp. Br., p. 54-55. These affiliates were not independent auditors, however. Both affiliates had joint venture agreements with Lucia and RJLC and drew substantial revenues from them. Tr. 445-46, 450. The affiliates, knowing the volume of leads generated by Lucia, which turned into revenue for them, could not be relied upon as true independent arbiters of the slideshow content. In 2003, while Ochs was with Securities America and reviewing Lucia's marketing material, she and her colleagues specifically requested that Lucia disclose the basis for the REIT return rates he used. Tr. 565; Resp. Ex. 20. There is no evidence that Lucia ever added those bases, and they do not appear anywhere in the slideshow. Div. Ex. 1. The '66 Backtest slides, unlike virtually every other section of the slideshow, bear no disclaimers at all, suggesting that there was in fact no advertising review of them. Div. Ex. 1, pp. 469-78. Furthermore, there is no evidence that anyone provided any support for the backtests to either affiliate, so that either would have a chance to consider the validity of the backtest slide figures.[35]

Respondents also cite to RJLC's internal compliance office to buttress the claim that the backtests were reasonable and in accordance with industry

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[35] In addition to ignoring compliance advice from its future chief compliance officer on the disclosure of the bases for REIT rates of return, one reason RJLC ended its relationship with Securities America was an unfavorable audit by Securities America, at least one of the subjects of which was the BOM strategy. Tr. 454-60.

standards. Resp. Br., p. 32. Ochs, RJLC's Chief Compliance Officer, seriously undermined that argument. Ochs, who was in charge of the office tasked with reviewing the slideshows, testified that she understood a backtest to be in accordance with the definition provided by the Division and its expert. Tr. 574-75. Thus, the head of Lucia's compliance department did not understand that Lucia's claimed "backtests" were not proper backtests. She could not have concurred that the slides were not misleading if she did not even understand the material. Additionally, Ochs came from Securities America were she had been part of a compliance team tasked with reviewing Lucia's marketing materials, including the slideshows. Tr. 445. Thus, two of the three levels of compliance review involved a common denominator in Ochs, who understood the term backtest to mean something different from what Lucia now offers. Tr. 575. Accordingly, little significance can be assigned to the compliance reviews.

Respondents' argument that the 2003 Commission review concluded that the "'73 Illustration slides did not violate securities laws" is unpersuasive. The Respondents point to no evidence that the Commission review made any such conclusion. The 2003 examination report stated only that RJLC did not advertise performance. Resp. Br., p. 19-20; Resp. Ex. 22, p. 3. That is a far cry from concluding the '73 Backtest did not violate securities laws. Moreover, it is not clear that the 2003 examiners asked for documentation of the backtest slide figures, which then comprised only the '73 Backtest, or that the examiners knew in 2003 that the slides were unsupported by any documentation, or that they examined any aspect of Respondents' REIT-connected activities. Resp. Ex.

22. It was only after Respondents produced a spreadsheet to OCIE in 2010, purportedly supporting the '73 Backtests, that OCIE knew how misleading the claims were. It was not reasonable for Respondents to assume, as they claim they did, that because the 2003 examination raised no issues regarding the '73 Backtest slides that the slides were not misleading. As noted, the '73 Backtest slides contained knowingly false statements regarding the assumptions behind the '73 Backtest; even if some of those assumptions were not charged as misrepresentations in this proceeding, Respondents could not possibly have believed that the '73 Backtest slides were not misleading. Even if the 2003 examination report (as opposed to the associated deficiency letter) had made such a conclusion, Respondents could not have relied upon it because they only received the examination report as part of discovery in this matter. Div. Reply, p. 52. Most significantly, the 2003 examination reviewed a version of the slideshow presentation that included only the '73 Backtest slides. Tr. 1484; Div. Ex. 21. That slideshow did not include the red flag-raising claim that the addition of REITs to a non-REIT BOM portfolio triples a portfolio's value, as the '66 Backtest does. Div. Ex. 21.

Slocum, where partial reliance on Commission examinations negated scienter, is inapplicable here. In Slocum, the defendants brought specific issues regarding account structure, which was later a basis of alleged fraud, to the Commission's attention during two examinations. 334 F. Supp. 2d at 160-61. Further, the defendants in Slocum relied upon the advice of counsel to structure its accounts, and after Commission and independent auditor recommendations regarding the specific account structures, tried to remedy them in accordance with those recommendations.

Id. at 159-60. Here, the 2003 examination did not focus upon the backtest issue, the issue was not specifically brought to the examiners' attention, and there is no evidence of reliance on advice of counsel.

4. Materiality

The Division proved that Lucia and RJLC's misrepresentations were material. The standard of materiality under Section 206 is whether or not a reasonable investor would have considered the information important in deciding whether or not to invest. See Basic, Inc. v. Levinson, 485 U.S. 224; 231-32, 240 (1988); TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976). Materiality is proved by showing a 'substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available.'" SEC v. Ginsburg, 362 F.3d 1292, 1302 (11th Cir. 2004) (quoting TSC Indus., 426 U.S. at 449 (1976)). Materiality does not require proof that accurate disclosure would have caused the reasonable investor to change his decision, but only that the omitted fact would have assumed actual significance in the deliberations of the reasonable investor. TSC Indus., 426 U.S. at 449.

A reasonable investor would consider the REIT investments in the backtests as dispositive proof that BOM with REITs was a wise investment choice. The contrasts between the fictional investor's "balanced" portfolio against the BOM portfolio with REITs, and the '66 Backtest without REITs against the '66 Backtest with REITs, could not have more clearly made the case for REITs. In the '73 Backtest, in contrast to the fictional investors without REITs, the fictional investors using BOM with REITs maintained a more than $1.5 million investment. According to the

'66 Backtest, a BOM portfolio without REITs would maintain a balance of $1.2 million after thirty-eight years while a BOM portfolio with REITs would be worth $4.7 million, more than triple the amount. Indeed, RJLC clients Richard DeSipio and Dennis Chisholm both testified that the discussion of REITs in their seminars was important in deciding to purchase non-traded REITs through RJLC. Tr. 281, 283, 380.

The use of an inflation rate much lower than historical rates, without disclosure that using historical rates would bankrupt the backtest portfolios, is plainly material. As demonstrated in Hekman's analysis, even a reduced inflation rate would cause the '66 Backtest to go bankrupt after 1993, ten years prior to the end of the backtest presented by Respondents, which, as presented, produced remarkable returns through 2003. Investors would surely not be interested in engaging RJLC as an adviser if they were told that the backtested portfolios went bankrupt after twenty or even twenty-eight years, especially because BOM was trumpeted as one that withstood the effects of inflation. Because Respondents' assumed stock returns differed between the Bold Bucketeers and the '73 Backtest, the '73 Backtest was not a demonstration that withdrawing safe money first is better regardless of the inflation rate; as noted, Respondents compared apples to oranges on this point, and in any event no documentary evidence of such a demonstration has surfaced. See Tr. 800. Inasmuch as the '73 Backtest was presented as such a demonstration during the seminars, it was materially misleading on that basis, as well.

In general, it is materially misleading to fail to disclose that advisory fees have not been deducted.

See F.X.C. Investors Corp., Initial Decision Release No. 218 (Dec. 9, 2002), 79 SEC Docket 472, 485. As noted, Respondents concede that advisory fees materially affect a portfolio's returns. Tr. 1199, 1203, 1285. Grenadier's expert report demonstrates the impact that inclusion of modest fees would have had upon the backtests. For example, modest fees on an index-tracking stock portfolio included in the '66 Backtest would have nearly halved the $4.7 million outcome to $2.5 million. Div. Ex. 70, pp. 15-16, Ex. 6a. Using similar fees would have quartered the final balance in the spreadsheet for the 1973 calculations. Id., Ex. 6b. Chisholm and DeSipio both testified that learning that the backtests failed to include fees would have been an important fact in their investment decisions. Tr. 289, 375-76.

It was material to fail to disclose that the backtested portfolios were not rebucketized or that they ended up being invested completely in stocks. Seminar attendees were led to believe that BOM would always maintain a safe income bucket to spend from before drawing from riskier investments. They were, further, advised against ever investing entirely in stocks. Attendees would, therefore, have wanted to know that the backtests supposedly proving the science behind BOM did not follow these basic principles, and that the positive results were largely attributable to fortunate timing of the stock market. Chisholm made clear that he would have found it important to know the facts about the bucket allocation following the first fourteen years of the backtests. Tr. 375.

a. Investment Decision

Lucia argues that SEC v. Goble, 682 F.3d 934 (11th Cir. 2012), precludes this action because RJLC's misrepresentations were not material. The court held

in Goble that misrepresentations influencing investors' choice of broker-dealer were not material because they did not encompass an investment decision. Id., at 944. In Goble, the defendant brokerage firm had misrepresented the level of its diminished capital reserves. The Commission's rationale for charging the defendant pursuant to Exchange Act Section 10(b) was that an investor client would consider it material whether its broker was solvent. Id. The court stated that such a rationale "cannot form the basis for [Section] 10(b) securities fraud liability." Id.

Lucia argues that, as in Goble, any misrepresentations would only influence a seminar attendee's decision to choose RJLC as an investment adviser, not to make a specific investment decision. To be sure, there is no evidence that RJLC or Lucia tried to sell specific securities at the seminars, nor are there any allegations by the Division that they did. But even assuming that the only basis for Lucia's violations of Sections 206(1) and 206(2) was that seminar attendees were influenced to choose RJLC as their investment adviser, Goble would not preclude liability. Advisers Act Section 206(1) and 206(2) do not share the requirement of Exchange Act Section 10(b) that misrepresentations occur "in connection with the purchase or sale of any security." Compare 15 U.S.C. § 78j(b) (Exchange Act Section 10(b)) with 15 U.S.C. § 80b-6 (Advisers Act Section 206). Though the basic test for materiality under the two statutes is similar, "[t]he elements for liability under . . . Section 10(b) and Rule 10b-5 of the Exchange Act . . . are more stringent than the requirements to violate Sections 206(1) and (2) of the Advisers Act." SEC v. Lauer, 2008 WL 4372896, at *24 (S.D. Fla. Sept. 24, 2008). "Congress intended the [Advisers Act] to be construed like other

securities legislation 'enacted for the purpose of avoiding frauds,' not technically and restrictively, but flexibly to effectuate its remedial purposes." SEC v. Capital Gains Bureau, Inc., 375 U.S. 180, 195 (1963).

It is well established that investment advisers may be held liable under the Advisers Act even without misrepresentations specific to a client investment decision. See, e.g., Vernazza, 327 F.3d at 859 (investment adviser's false representations of conflicts of interest in its Form ADV filed with the Commission was material); SEC v. K.W. Brown & Co., 555 F. Supp. 2d 1275, 1308 (S.D. Fla. December 19, 2007) (investment adviser's scheme extending gains in favor of preferred clients while passing along losses to other clients was material because it was determinative as to whether clients would invest their money and trust with the defendant)[36]; SEC v. Moran, 922 F. Supp. 867, 896 (S.D.N.Y. 1996) (defendant investment adviser's insider trading scheme allocated higher-priced shares to client accounts than its own, to the detriment of firm clients). Accordingly, Goble does not bar liability here.

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[36] K.W. Brown cited to Applicability of the Investment Advisers Act to Financial Planners, Pension Consultants, and Other Persons Who Provide Investment Advisory Services as a Component of Other Financial Services, Investment Advisers Act Release No. 1092 (Oct. 8, 1987), 39 SEC Docket 653, an interpretive release by the Commission, which stated that "the Commission has applied Sections 206(1) and 206(2) in circumstances in which the fraudulent conduct arose out of the investment advisory relationship between an investment adviser and its clients, even though the conduct does not involve a securities transaction." Id., at 670-71.

b. Omission of Material Fact

Respondents never warned that REIT rates, for example, were hypothetical and not historically accurate, a material omission of fact. Respondents cite to disclaimer language used throughout the slideshows and invoked by Lucia in his narration as evidence that audience members could not have been misled, and that they would understand that the rates used for the backtests were entirely hypothetical. Resp. Br., p. 2 n.2. As noted supra, though, the slideshow's assertions regarding REITs were misleading in multiple ways, including that they suggested that REITs were reasonably available as investments as far back as "the sixties." Div. Ex. 66, p. 44. A reasonable investor would have wanted to know that REITs were not available at that time, and that REIT returns were not merely "hypothetical," as the slideshow states, but effectively nonexistent. Additionally, the most frequently used disclaimer throughout the slideshow, including during the backtests, was that the slideshow was representing hypothetical investments and that past performance was not indicative of future returns. Div. Ex. 1; Tr. 227, 567. The proceeding does not allege that Lucia used actual examples, or that by using the backtests, he was guaranteeing future returns, which is what the disclaimers warned. Even if the disclaimers had been more direct, general cautionary language does not render omission of a specific misleading historical fact immaterial. See SEC v. Merchant Capital, LLC, 483 F.3d 747, 768 (11th Cir. 2007) (citing In re Westinghouse Sec. Litig., 90 F.3d 696, 710 (3d Cir. 1996)); Klein v. First Western Gov't Securities, Inc., 24 F.3d 480, 489 (3d Cir. 1994).

B. Section 206(4) of the Advisers Act

Section 206(4) of the Advisers Act prohibits engaging in "any act, practice, or course of business that is fraudulent, deceptive, or manipulative," and authorizes the Commission to prescribe rules designed to prevent such conduct. 15 U.S.C. § 80b-6(4). As with Section 206(2), which prohibits engaging in "any transaction, practice, or course of business which operates as a fraud or deceit," scienter need not be proven under Section 206(4). 15 U.S.C. § 80b-6(2); Capital Gains Research Bureau, 375 U.S. at 195.

Just as Respondents' misrepresentations constituted a practice or course of business which operated as a fraud or deceit under Section 206(2), they also constituted a practice or course of business that was fraudulent and deceptive under Section 206(4). Accordingly, Respondents violated Section 206(4).[37]

Rule 206(4)-1(a)(5) makes it a fraudulent, deceptive, or manipulative act, practice, or course of business within the meaning of Section 206(4) for a registered investment adviser to publish, circulate, or distribute any advertisement "[w]hich contains any untrue statement of a material fact, or which is otherwise false or misleading." 17 C.F.R. § 275.206(4)-1(a)(5). Conduct under this Rule must be measured from the viewpoint of a person unskilled and unsophisticated in investment matters. See SEC v. C.R. Richmond & Co., 565 F.2d 1101, 1104-05 (9th Cir.

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[37] Violation of one of its associated Rules is not a precondition to finding a violation of Section 206(4). See Warwick Capital Mgmt., Inc., Advisers Act Release No. 2694 (Jan. 16, 2008), 92 SEC Docket 1410, 1411 n.3 (finding a violation of Section 206(4) without an associated violation of Rule 206(4)-1(a)(5)).

1977). Scienter is not an element. See Capital Gains Research Bureau, 375 U.S. at 195.

The Division alleges that the backtests constituted misleading performance advertising, a sub-category of prohibited Rule 206(4)-1(a)(5) advertisements. I find that Respondents' seminar presentations do not qualify as advertising, and are therefore not performance advertising. Rule 206(4)-1(b) defines what specific types of advertisements are included under Rule 206(4)-1(a). The term "advertisement" includes "written communication[s] addressed to more than one person . . . or any notice or other announcement in any publication or by radio or television." 17 C.F.R. § 275.206(4)-1(b). The concept of advertisement has been construed liberally, and includes "investment advisory material which promotes advisory services for the purpose of inducing potential clients to subscribe to those services." C.R. Richmond, 565 F.2d at 1105.

Lucia disseminated his misrepresentations in his books and through his radio and television shows, as well as via seminars and at least one webinar. Tr. 1025-26; Div. Exs. 66-69. At the seminars, various printed materials were distributed, but they do not appear to have been summaries of the BOM strategy. Tr. 1052-55. The OIP asserts that Lucia promoted the BOM strategy on "his radio show and website, at seminars, and in his books." OIP, pp. 2-4. Nonetheless, the core allegation of the OIP is that "it was materially misleading for Respondents to claim that their alleged backtesting validated the BOM strategy," after which the OIP almost exclusively discusses the slideshow. OIP, pp. 7-9.

Consequently, there is some doubt about whether the OIP provides fair notice to Respondents that they

stand accused of violating Rule 206(4)-1(a)(5) by misrepresentations other than those made at the seminars. In view of the limited scope of the Division's argument in its post-hearing brief on this point – only that "Respondents' seminar slideshow is an advertisement within the meaning of the Rule" – I conclude that only misrepresentations at the seminars may be found violative of Rule 206(4)-1(a)(5). Div. Br., p. 40.

Given this limitation, the Division has not proven that "written communications" include live slideshow presentations. The precedent, outdated as it may be, holds written communications to include only traditional media, including books, newsletters, and newspaper and magazine advertisements. See, e.g., SEC v. Suter, No. 81-3865, 1983 WL 1287, *12 (N.D. Ill. Feb. 11, 1983) (newsletters); SEC v. Lindsey-Holman Co., No. 78-54-MAC, 1978 WL 1129 (M.D. Ga. Aug. 6, 1978) (newspaper advertisements); C.R. Richmond, 565 F.2d at 1104 (books and newsletters). There is no evidence that slideshow printouts or synopses thereof were handed out to seminar participants or otherwise published in printed or handwritten form at the seminars. I do not find that the slideshow presentations were "written communications" as that term has been interpreted. Accordingly, Respondents did not violate Rule 206(4)-1(a)(5).

C. Section 204 of the Advisers Act

Advisers Act Section 204 requires investment advisers to "make and keep for prescribed periods such records . . . as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 80b-4(a). Advisers Act Rule 204-2(a)(16) requires investment advisers to keep true and accurate record of:

> All accounts, books, internal working papers, and any other records or documents that are necessary to form the basis for or demonstrate the calculation of the performance or rate of return of any or all managed accounts or securities recommendations in any notice, circular, advertisement, newspaper article, investment letter, bulletin or other communication that the investment adviser circulates or distributes, directly or indirectly, to 10 or more persons (other than persons connected with such investment adviser); provided, however, that, with respect to the performance of managed accounts, the retention of all account statements, if they reflect all debits, credits, and other transactions in a client's account for the period of the statement, and all worksheets necessary to demonstrate the calculation of the performance or rate of return of all managed accounts shall be deemed to satisfy the requirements of this paragraph.

17 C.F.R. § 275.204-2(a)(16). The plain language of the Rule encompasses only advertisements of performance or rates of return for managed accounts or specific securities recommendations. Though Lucia's seminars influenced individuals to purchase classes of securities from RJLC, particularly non-traded REITS, Lucia never advertised a specific security, nor is there evidence that the examples used in the slideshow were specific managed accounts. The same is true of the Webinar. Div. Br., p. 44 n.12. Accordingly, Lucia was not required to maintain the above-referenced

records, and did not violate either Section 204 or Rule 204-2(a)(16) thereunder.[38]

D. Aiding and Abetting

Lucia willfully aided and abetted RJLC's violations of Sections 206(1), 206(4), and 206(2) of the Advisers Act. To establish a claim of aiding and abetting there must be: (1) a primary violation of the securities laws; (2) knowledge of the primary violation by the aider and abettor; and (3) substantial assistance by the aider and abettor in the commission of the primary violation. SEC v. DiBella, 587 F.3d 553, 566 (2d Cir. 2009). Lucia acted with scienter, and provided much more than substantial assistance. He was not only the controlling sole shareholder of RJLC, but he was the creator of the slideshow, the seminar marketing, the backtests, and all of the components to the backtest, including the REIT rates, the length and timing of the REIT investments, and the historical periods to use as context. The finding that RJLC violated Sections 206(1), 206(2), and 206(4) of the Advisers Act inescapably leads to a finding that Lucia aided and abetted it.

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[38] In contrast to Section 206(4), the language of Section 204 suggests that it may only be violated if one of its associated Rules is violated. 15 U.S.C. § 80b-4(a) ("as the Commission, by rule, may prescribe" (emphasis added)). In any event, the Division makes no argument regarding Section 204 separate from its argument regarding Rule 204-2(a)(16). Div. Br., pp. 43-44. I therefore find no separate violation of Section 204. Additionally, not being required to comply with this particular Rule is not mutually exclusive with Respondents' violations of Sections 206(1), 206(2), and 206(4) of the Advisers Act. That Respondents failed to properly maintain records is relevant at least to evaluating scienter and determining whether their statements were misleading, even though their failure was not a technical violation of the Rule.

E. Affirmative Defenses

1. Statute of Limitations

Respondents included as an affirmative defense that this proceeding is barred by the five-year statute of limitations for fraud claims, codified at 28 U.S.C. § 2462, because the violations were discovered, or should have been discovered, during the Commission's review in 2003. Lucia Answer, p. 8; RJLC Answer, p. 8; Resp. Br., p. 69. Under Gabelli v. SEC, 133 S.Ct. 1216, 1220-21 (2013), the statute of limitations clock begins running at time of accrual, that is, when the cause of action becomes enforceable. Each presentation of the misleading slideshow was a separate and distinct violation, and any resulting cause of action could not have accrued until the presentation occurred. See David Henry Disraeli, Exchange Act Release No. 57027 (Dec. 21, 2007), 92 SEC Docket 852, 875 (multiple material misrepresentations and omissions constituted "repeated violations"); Warwick Capital Mgmt., Inc., 92 SEC Docket at 1427 ("repeated instances of egregious . . . behavior" violative of Sections 206(1), 206(2), and 206(4)). The limitations clock thus runs from each violative presentation, not from the date of the first violative presentation.

In any event, the statute of limitations does not apply to this entire proceeding, but only to particular sanctions, specifically, civil penalties and any associational bar. See Gregory O. Trautman, Exchange Act Release No. 61167 (Dec. 15, 2009), 97 SEC Docket 23492, 23525-26.[39] The OIP makes no allegations regarding the time period, so it is important to consider

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[39] An amended version of this Commission Opinion is available only on the Commission's website. In pertinent part, it is materially identical to the printed Release.

when these acts occurred in evaluating those sanctions. As the record shows, Lucia has been giving some semblance of the BOM slideshow presentation since 2000, and was presenting the backtest slides as late as December 2010, when Respondents received OCIE's deficiency letter. Because each presentation was a new unlawful act, the clock began running anew each time Lucia presented the slideshow. The OIP was filed on September 5, 2012, and thus, seminars occurring any time after September 5, 2007, five years prior, can be considered in this proceeding as to those issues affected by the statute of limitations.

2. Due Process

Respondents present two due process arguments: (1) that their rights were violated because the formal order of investigation (FOI) was approved while the OCIE examination was ongoing, and (2) that they lacked fair notice that their conduct was proscribed. Resp. Br., pp. 22-25, 66-69. It is not clear whether I have the authority to even entertain such due process claims. See Gregory M. Dearlove, CPA, Exchange Act Release No. 57244 (Jan. 31, 2008), 92 SEC Docket 1867, 1920-21, 1926 (resolving the claim that the Commission's Rules of Practice violated due process, an issue that the ALJ had declined to address as a matter better left to the Commission), pet. denied, 573 F.3d 801 (D.C. Cir. 2009). Assuming that I do have such authority, I conclude that Respondents' due process arguments lack merit.

First, Respondents argue that the investigation in this matter violated their due process rights because the FOI was approved on December 2, 2010, fifteen days before the December 17, 2010 deficiency letter issued, but Respondents did not learn of the FOI until May 11, 2011. Resp. Br., p. 24. However, due process

does not require notice, either actual or constructive, of an administrative investigation into possible violations of the securities laws. RNR Enters., Inc. v. SEC, 122 F.3d 93, 98 (2d Cir. 1997) (quoting Gold v. SEC, 48 F.3d 987, 991 (7th Cir. 1995)). The timing of the FOI may have been unusual or irregular, but neither party has pointed to any authority addressing that issue. Certainly, Rule 7(a) of the Commission's Rules Relating to Investigations, which by its own terms applies only to formal investigative proceedings, as opposed to examinations, does not require the Division to inform a party of its investigation merely because OCIE is simultaneously conducting a lawful examination of that party. See 17 C.F.R. § 203.7(a). Moreover, Respondents have shown no prejudice arising from the timing of the FOI. The evidence is uncontroverted that the Division did not use OCIE's examination as a "stalking horse" to obtain evidence outside the normal investigative process. Tr. 214. Respondents had a choice: respond to the deficiency letter or not. This choice would have been the same whether or not they had been aware of the investigation, and whatever response they made would have been just as accessible to the Division regardless of when the FOI issued. Respondents, as registered investment advisers, were required by law to cooperate with OCIE and provide documentation as needed. See 15 U.S.C. § 80b-4(a). It seems unlikely that, even if provided with the FOI, Respondents would have chosen to stop cooperating with OCIE, nor have they identified any particular thing that they would have done differently in that situation.

Second, Respondents cannot "credibly claim lack of fair notice of the proscription against defrauding investors." Valicenti Advisory Servs., Inc. v. SEC, 198 F.3d 62, 66 (2d Cir. 1999). Respondents nevertheless

offer four arguments in support of their contention that they lacked reasonable notice that their conduct was unlawful, none of which I find persuasive. Resp. Br., pp. 66-69. First, as discussed above in connection with Rule 204-2(a)(16), the slideshows did not constitute performance advertising, so any vagueness about the law of performance advertising is irrelevant. Second, even assuming that the slideshows "comport with industry standards" in part, they are also materially misleading, which is obviously not an industry standard. Id., p. 68. Third, the OIP alleges that "it was materially misleading for Respondents to claim that their alleged backtesting validated the BOM strategy," that is, Respondents are charged with making materially misleading factual assertions and omissions, including as to a particular security, non-traded REITs. OIP, p. 7. Respondents' assertion that they have been "prosecuted . . . for hypothetical illustrations which are a comparison of withdrawal strategies unrelated to any managed account or security," is simply false. Resp. Br., p. 68. Fourth, the 2003 slideshow devotes at most five slides to the 1973 backtest, has no discussion of backtesting to 1966, and does not compare REIT and non-REIT investment. Div. Ex. 21, pp. 74-76. The 2009-10 slideshow, by contrast, devotes thirteen slides to the backtests, discusses backtesting to 1966, and shows the alleged advantages of investing in REITs by comparing investments with and without them. Div. Ex. 1, pp. 466-78. The 2003 slideshow did not possess "identical issues to those in the OIP," and the OIP does not constitute a "change of course." Resp. Br., p. 68.

3. Other Defenses

Respondents' Answers originally included eight affirmative defenses, but the defenses of waiver and

unclean hands were stricken by Order on November 7, 2012. Except for the seventh affirmative defense, addressed infra, Respondents apparently found insufficient merit in the remaining affirmative defenses to justify addressing them in their post-hearing brief or reply. I, too, find insufficient merit in them to warrant discussion.

V. SANCTIONS

The Division requests that Lucia be barred from association with any investment adviser and broker-dealer, that Lucia and RJLC have their investment adviser registrations revoked, that they be ordered to cease and desist from further violations of the securities laws, and that they be required to pay civil money penalties of $150,000 and $725,000, respectively. Div. Br., pp. 46-47. The Division also requests that Lucia be required to "disclose at any future seminars that he has been sanctioned for providing misleading performance data about the BOM portfolio strategy." Id., p. 47.

The sanctions listed below are unchanged from the July 8, 2013, Initial Decision, in which I stated that even if there were violations resulting from the misrepresentations the OIP charged that I did not address, the sanction would remain the same. I had already ordered the severest sanctions available for the requested collateral bar and registration revocation, and I issued a cease-and-desist order. In view of Respondents' additional proven misrepresentations, I see no reason to change those sanctions. The only other different sanction available is in the civil penalty amount. Although the egregiousness of Respondents' conduct is greater in light of the additional proven misrepresentations, I continue to find that the mitigating factors weigh in favor of civil penalties of

approximately one third of the maximum. I therefore reconfirm the penalty amounts in the July 8, 2013, Initial Decision.

A. Willful Violations and the Public Interest

The Division seeks sanctions pursuant to Section 15(b) of the Exchange Act and Sections 203(e), 203(f), 203(i), and 203(k) of the Advisers Act. OIP, p. 10; Div. Br., pp. 44-47. To impose sanctions under some of these sections, Respondent's violations must be willful. 15 U.S.C. § 78o(b)(6)(A)(i); 15 U.S.C. §§ 80b-3(e), (f), & (i) (2010); see also Rapoport v. SEC, 682 F.3d 98, 108 (D.C. Cir. 2012). A finding of willfulness does not require intent to violate the law, but merely intent to do the act which constitutes a violation of the law. Wonsover v. SEC, 205 F.3d 408, 414 (D.C. Cir. 2000); Arthur Lipper Corp. v. SEC, 547 F.2d 171, 180 (2d Cir. 1976).

Lucia and RJLC acted willfully. Lucia's statements were not the result of a mistake or clerical error, they were made voluntarily and knowingly. See Wonsover, 205 F.3d at 413-15. As Lucia testified, he worked on the backtests and authored the slideshows. Tr. 1066-67, 1089, 1095. Therefore, Lucia acted willfully, and as its controlling person, his willfulness is imputed to RJLC.

When considering whether an administrative sanction serves the public interest, the Commission considers the factors identified in Steadman v. SEC, 603 F.2d 1126, 1140 (5th Cir. 1979), aff'd on other grounds, 450 U.S. 91 (1981): the egregiousness of the respondent's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the respondent's assurances against future violations, the respondent's recognition of the

wrongful nature of his or her conduct, and the likelihood that the respondent's occupation will present opportunities for future violations (Steadman factors). Gary M. Kornman, Advisers Act Release No. 2840 (Feb. 13, 2009), 95 SEC Docket 14246, 14255, pet. denied, 592 F.3d 173 (D.C. Cir. 2010). The Commission also considers the extent to which the sanction will have a deterrent effect. See Schield Mgmt. Co., Exchange Act Release No. 53201 (Jan. 31, 2006), 87 SEC Docket 848, 862 & n.46 (citations omitted). The Commission's inquiry into the appropriate sanction to protect the public interest is a flexible one, and no one factor is dispositive. See Gary M. Kornman, 95 SEC Docket at 14255.

In this case the public interest factors weigh in favor of a heavy sanction. Lucia has over thirty-eight years of experience as an investment adviser. He knew his fiduciary obligations as an investment adviser and he knew that he was violating them by misleading prospective clients. He and RJLC became very financially successful as a result. He committed these violations many times between 2007 and 2010. Thus, Respondents' violative behavior was egregious, recurrent, and performed with scienter. Respondents have utterly failed to recognize the wrongful nature of their conduct. Lucia's current occupation as an investment adviser and media presence, and RJLC's registration, provide immediate opportunities to repeat the violations.

To his credit, Lucia has made efforts to end the violative conduct. However, following the 2003 deficiency letter, RJLC informed the Commission, in writing, that it would cease using misleading figures regarding the longevity of the firm, the number of clients serviced, and the amount of assets managed.

Resp. Ex. 14. Despite those assurances, RJLC continued using those figures until OCIE discovered them and noted them in the 2010 deficiency letter. Div. Ex. 2. This is probably because they did not consider the figures misleading. Resp. Ex. 7. Respondents' inability to keep their promises to OCIE undercuts the credibility of similar assurances going forward. Admittedly, Respondents stopped using the backtest slides and recalled Lucia's books after OCIE's 2010 deficiency letter. Tr. 1275-77. Nevertheless, Respondents have demonstrated an inability to sustain such compliance efforts long term, and I find that they have not made sufficiently sincere assurances against future violations. Accordingly, all of the Steadman factors weigh against Respondents and in favor of a severe sanction.

B. Revocation of Investment Adviser Registrations

Section 203(e) of the Advisers Act authorizes the Commission to revoke an investment adviser's registration if it, or any person associated with it, has willfully violated, or willfully aided and abetted the violation of, any provision of the Advisers Act, and if revocation is in the public interest. In light of the Steadman Factors, Respondents must not be allowed to continue to serve as investment advisers, and their registrations will be permanently revoked.

C. Associational Bars

Section 203(f) of the Advisers Act authorizes the Commission to bar or suspend a person from association with an investment adviser for willful violations of the Advisers Act, if it is in the public interest. 15 U.S.C. § 80b-3(f). Section 15(b)(6) of the Exchange Act similarly authorizes the Commission to bar a person

from association with any broker or dealer, if the person has willfully violated any provision of the Advisers Act and it is in the public interest. 15 U.S.C. § 78o(b)(6)(A)(i); John W. Lawton, Advisers Act Release No. 3513 (Dec. 13, 2012), 105 SEC Docket 61722, 61737.[40]

Again, all Steadman factors weigh in favor of a permanent associational bar. Furthermore, it is in the Commission's interest to deter others from behaving like Lucia. In addition to intentionally misleading clients and prospective clients, Lucia refused to accept responsibility for the abdication of his fiduciary duty to his clients. He now tries to shift partial blame to the Commission for failing to detect problems in the 2003 slideshow. Therefore, it is in the public interest to permanently bar Lucia from association with investment advisers, brokers, and dealers.

D. Cease-And-Desist

Advisers Act Section 203(k) authorizes the Commission to impose a cease-and-desist order for violations of the Advisers Act. See 15 U.S.C. §§ 80b-3(k). The Commission requires some likelihood of future violation before imposing a cease-and-desist order. KPMG Peat Marwick LLP, Exchange Act Release No. 43862 (Jan. 19, 2001), 54 S.E.C 1135, 1185, motion for reconsideration denied, Exchange Act Release No. 44050 (Mar. 5, 2001), 53 S.E.C. 1, pet. denied, 289 F.3d 109 (D.C. Cir. 2002). However, "a finding of a [past] violation raises a sufficient risk of future viola-

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[40] A broker-dealer bar in this case is, alternatively, direct (assuming Lucia is affiliated with Lucia Securities or seeks to become so in the future) or collateral (assuming Lucia is considered not affiliated with Lucia Securities).

tion," because "evidence showing that a respondent violated the law once probably also shows a risk of repetition that merits our ordering him to cease and desist." Id. at 1185.

Respondents' egregious and repetitive misconduct in providing thousands of potential investor clients with misleading information, Lucia's current employment as an investment adviser and media presence, and his inability to satisfy his previous assurances against violative conduct presents sufficient risk of future violations. Respondents claim to have already ceased their violative conduct, which is the subject of their seventh affirmative defense. Tr. 1275-77; RJLC Answer, p. 8. Even assuming this is true, it is of little consequence. See Geiger v. SEC, 363 F.3d 481, 489 (D.C. Cir. 2004) (a single violation raises an inference that it will be repeated, especially when the misconduct is egregious and when the violator thinks he did nothing wrong); see also Hunter Adams, Exchange Act Release No. 51117 (Feb. 1, 2005), 84 SEC Docket 2928, 2929 n.6 (listing reasons why even duplicative injunctive relief may be warranted). Therefore, the imposition of a cease-and-desist order is warranted. In view of the fact that the associational bar and investment adviser registration revocation will presumably put Lucia out of business, I see no need to add the condition that Respondents disclose at any future seminars that they have been sanctioned for providing misleading performance data about BOM.

E. Civil Penalty

Under Section 203(i) of the Advisers Act, the Commission may impose a civil money penalty if a respondent willfully violated any provision of the Advisers Act, and if such penalty is in the public interest. 15 U.S.C. §§ 80b-3(i).

A three-tier system establishes the maximum civil money penalty that may be imposed for each violation found. Id. Where a respondent's misconduct involve fraud, deceit, or deliberate or reckless disregard of a regulatory requirement, and resulted in substantial pecuniary gain, the Commission may impose a "Third-Tier" penalty of up to $150,000 for each act or omission by an individual and $725,000 for an entity. Id.; 17 C.F.R. § 201.1004 (adjusting the statutory amounts for inflation). Within any particular tier, the Commission has the discretion to set the amount of the penalty. See Brendan E. Murray, Advisers Act Release No. 2809 (Nov. 21, 2008), 94 SEC Docket 11961, 11978; The Rockies Fund, Inc., Advisers Act Release No. 54892 (Dec. 7, 2006), 89 SEC Docket 1517, 1528.

In determining whether a penalty is in the public interest, the Commission may consider (1) whether the violation involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement, (2) the resulting harm to other persons, (3) any unjust enrichment and prior restitution, (4) the respondent's prior regulatory record, (5) the need to deter the respondent and other persons, and (6) such other matters as justice may require. 15 U.S.C. § 80b-3(i); Murray, 94 SEC Docket at 11978.

I find a third-tier penalty to be warranted and in the public interest. Respondents acted deceitfully and disregarded the law intentionally. This factor is particularly important given the recurrence of Respondents' deceitful conduct, and the substantial financial success Respondents have enjoyed at their clients' expense. Also, the need to deter Respondents is strong, given Lucia's continued employment in the financial sector and his failure to acknowledge the wrongfulness of his conduct. See Murray, 94 SEC Docket at

11978. Sanctions imposed on Respondents will also deter others from engaging in the same misconduct. Id.

Nonetheless, the Division's requested penalty is excessive. Although the tier determines the maximum penalty, "each case has its own particular facts and circumstances which determine the appropriate penalty to be imposed" within the tier. SEC v. Murray, No. OS-CV-4643 (MKB), 2013 WL 839840, at *3 (E.D.N.Y. Mar. 6, 2013) (quotation omitted); see also SEC v. Kern, 425 F.3d 143, 153 (2d Cir. 2005). In addition to the statutory factors cited above, courts consider:

> (1) the egregiousness of the violations at issue, (2) defendants' scienter, (3) the repeated nature of the violations, (4) defendants' failure to admit to their wrongdoing; (5) whether defendants' conduct created substantial losses or the risk of substantial losses to other persons; (6) defendants' lack of cooperation and honesty with authorities, if any; and (7) whether the penalty that would otherwise be appropriate should be reduced due to [respondents'] demonstrated current and future financial condition.

SEC v. Lybrand, 281 F. Supp. 2d 726, 730 (S.D.N.Y. 2003), aff'd on other grounds, 425 F.3d 143 (2d Cir. 2005) (Lybrand factors).

Most of the Lybrand factors weigh in favor of a severe sanction. Nonetheless, although the "dissemination of false and misleading financial information by its nature causes serious harm to investors and the marketplace," in this case the evidence of actual losses to individual investors is virtually nonexistent. The

Rockies Fund, 89 SEC Docket at 1527. Chisholm complained of being unable to liquidate his REIT, and DeSipio filed an arbitration which was later dismissed. But there is no evidence of the amount of any unjust enrichment as to any particular investor. Additionally, Respondents have a clean regulatory record and were cooperative with examiners and investigators. Accordingly, I believe the maximum civil penalty is too high, and a civil penalty of about one-third of the maximum is justified.

The Division requests that the third-tier civil penalty be imposed one time, for each Respondent. While the statute provides that a penalty may be imposed for "each act or omission," it leaves the precise unit of violation undefined. See Colin S. Diver, The Assessment and Mitigation of Civil Money Penalties by Federal Administrative Agencies, 79 Colum. L. Rev. 1435, 1440-41 (1979). Although Respondents technically violated the statute hundreds of times, a one-time penalty prejudices them the least.[41] Therefore, a one-time, third-tier $250,000 penalty for RJLC and $50,000 penalty for Lucia is warranted.

TRANSCRIPT CORRECTIONS

On February 1, 2013, Respondents submitted a Motion re Proposed Transcript Corrections to the Hearing Transcript (Transcript Motion). The Division filed its Objections thereto on February 25, 2013. Respondents did not file a reply.

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[41] Assuming, hypothetically, that Lucia gave forty seminars a year for the three years actionable under the statute of limitations, at most RJLC would be subject to an $87 million penalty and Lucia would be subject to an $18 million penalty. Such penalties would plainly be disproportionate and unreasonable.

With two exceptions, the proposed corrections generally pertain to clear typographic or scrivener's errors, and they will be adopted. The first exception is the proposed change of "were back tests" to "were not back tests," in a statement made by Respondents' counsel in reference to Bennett's testimony. Transcript Motion, p. 1 (citing Tr. 209:17). Although I agree with the Division that the referenced testimony is found at Tr. 99:25-100:3, I do not agree that the proposed change would mischaracterize Bennett's testimony. To the contrary, the proposed change would harmonize Respondents' counsel's statement with Bennett's testimony. The second exception is the proposed change of "him" to "me" on one page. Tr. 792:17. In fact, the transcript already says "me," and in context the word should clearly read "him." Id. Accordingly, the Transcript Motion is granted in part, the proposed corrections are adopted as outlined above, and the "me" on page 792, line 17 is ordered changed to "him."

RECORD CERTIFICATION

Pursuant to Rule 351(b) of the Commission's Rules of Practice, 17 C.F.R. § 201.351(b), I certify that the record includes the items set forth in the Record Index issued by the Secretary of the Commission on April 19, 2013, and five documents filed since then: the July 8, 2013, Initial Decision; Respondents' Motion to Correct Manifest Errors of Fact, filed July 18, 2013; the Division's Opposition thereto, filed July 25, 2013; my Order on Motion to Correct Manifest Errors of Fact, filed August 7, 2013; and the Remand Order, filed August 8, 2013.

ORDER

IT IS ORDERED that, pursuant to Section 203(e) of the Advisers Act, the registrations of Raymond J. Lucia Companies, Inc. and Raymond J. Lucia, Sr. as investment advisers are REVOKED.

IT IS FURTHER ORDERED that, pursuant to Section 203(f) of the Advisers Act and Section 15(b) of the Exchange Act, Raymond J. Lucia, Sr. is permanently BARRED from association with investment advisers, brokers, or dealers.

IT IS FURTHER ORDERED that, pursuant to Section 203(k) of the Advisers Act, Raymond J. Lucia Companies, Inc. shall CEASE AND DESIST from committing, and Raymond J. Lucia, Sr. shall CEASE AND DESIST from aiding and abetting or causing the commission of, any violations or future violations of Sections 206(1), 206(2), and 206(4) of the Advisers Act.

IT IS FURTHER ORDERED that, pursuant to Section 203(i) of the Advisers Act, Raymond J. Lucia, Sr. shall PAY A CIVIL MONEY PENALTY in the amount of $50,000.

IT IS FURTHER ORDERED that, pursuant to Section 203(i) of the Advisers Act, Raymond J. Lucia Companies, Inc. shall PAY A CIVIL MONEY PENALTY in the amount of $250,000.

IT IS FURTHER ORDERED that Respondents' Motion re Proposed Transcript Corrections to the Hearing Transcript is GRANTED IN PART, all proposed corrections except the proposed correction to page 792, line 17, are adopted, and the "me" on page 792, line 17 of the transcript is ORDERED changed to "him.".

Payment of penalties and disgorgement plus prejudgment interest shall be made on the first day following the day this Initial Decision becomes final. Payment shall be made by certified check, United States postal money order, bank cashier's check, wire transfer, or bank money order, payable to the Securities and Exchange Commission. The payment, and a cover letter identifying the Respondent(s) and Administrative Proceeding No. 3-15006, shall be delivered to: Enterprises Services Center, Accounts Receivable Branch, HQ Bldg., Room 181, AMZ-341, 6500 South MacArthur Bld., Oklahoma City, Oklahoma 73169. A copy of the cover letter and instrument of payment shall be sent to the Commission's Division of Enforcement, directed to the attention of counsel of record.

This Initial Decision shall become effective in accordance with and subject to the provisions of Rule 360 of the Commission's Rules of Practice, 17 C.F.R. § 201.360. Pursuant to that Rule, a party may file a petition for review of this Initial Decision within twenty-one days after service of the Initial Decision. A party may also file a motion to correct a manifest error of fact within ten days of the Initial Decision, pursuant to Rule 111 of the Commission's Rules of Practice, 17 C.F.R. § 201.111. If a motion to correct a manifest error of fact is filed by a party, then that party shall have twenty-one days to file a petition for review from the date of the undersigned's order resolving such motion to correct manifest error of fact. The Initial Decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or motion to correct manifest error of fact or the Commission determines on its own initiative to review the In-

itial Decision as to a party. If any of these events occur, the Initial Decision shall not become final as to that party.

Cameron Elliot
Administrative Law Judge

APPENDIX F

ADMINISTRATIVE PROCEEDING
File No. 3-15006

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION
August 8, 2013

In the Matter of RAYMOND J. LUCIA COMPANIES, INC. and RAYMOND J. LUCIA, SR.	ORDER REMANDING CASE FOR ISSUANCE OF AN INITIAL DECISION PURSUANT TO RULE OF PRACTICE 360

On September 5, 2012, the Commission instituted administrative proceedings against the above-named respondents pursuant to Section 15(b) of the Securities Exchange Act of 1934, Sections 203(e), 203(f), and 203(k) of the Investment Advisers Act of 1940, and Section 9(b) of the Investment Company Act of 1940.[1] On July 8, 2013, the administrative law judge issued an Initial Decision concluding that Raymond J. Lucia Companies, Inc. ("RJLC"), a registered investment adviser had violated Sections 206(1), 206(2), and 206(4) of the Advisers Act and that Raymond J. Lucia, RJLC's sole owner and also a registered investment

[1] *Raymond J. Lucia Cos.*, Exchange Act Rel. No. 67781, Advisers Act Rel. No. 3456, Investment Company Act Rel. No. 30193, 2012 WL 3838150 (Sept. 5, 2012); *see* 15 U.S.C. §§ 78o(b), 80a-9(b), 80b-3(e), 80b-3(f), 80b-3(k).

adviser, had willfully aided and abetted those violations.[2]

The time for the parties to petition for review of the Initial Decision has not yet expired.[3] On our own initiative, we have determined that it is appropriate to remand the matter to the law judge for further consideration because the Initial Decision did not make findings with respect to all of the material allegations set forth in the Order Instituting Proceedings ("OIP") and presented for decision by the parties.

The OIP alleged that Respondents misrepresented to prospective investors the validity of the backtesting that they performed on their "Buckets of Money" ("BOM") investment strategy.[4] It identified four principal respects in which Respondents' backtesting allegedly was misleading. *First*, Respondents used a hypothetical 3% inflation rate, which was lower than the historically accurate inflation rates that prevailed during the 1970s and 1980s.[5] *Second*, Respondents used hypothetical rates of return for real estate investment trusts ("REITs") without disclosing that such returns would not have been available.[6] *Third*, Respondents did not disclose that the backtested returns did not take into account advisory

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[2] *Raymond J. Lucia Cos.*, Initial Decision Rel. No. 495, 2013 WL 3379719 (July 8, 2013).

[3] Rule of Practice 410(b) provides that a petition for review "shall be filed with the Commission within such time after service of the initial decision as prescribed by the hearing officer . . . unless a party has filed a motion to correct an initial decision with the hearing officer," which Respondents did here. 17 C.F.R. § 201.410(b).

[4] OIP ¶ 5.

[5] *Id.* ¶¶ 19-20, 22.

[6] *Id.* ¶¶ 21-22.

fees.[7] *Fourth*, Respondents did not disclose that the backtested portfolios had not been reallocated between asset categories over time in accordance with the BOM strategy.[8]

In view of these allegations, we deemed "it necessary and appropriate in the public interest that public administrative and cease-and-desist proceedings be instituted to determine," *inter alia*, "[w]hether the allegations set forth [in the OIP] . . . are true and, in connection therewith, to afford Respondents an opportunity to establish any defenses to such allegations."[9] We directed the law judge to issue an initial decision no later than 300 days from the date of service of the OIP pursuant to Rule 360(a)(2) of the Rules of Practice.[10]

After a nine-day hearing, the parties submitted post-hearing briefs that addressed at length each of the claims set forth in the OIP.[11] Yet the Initial Decision made findings with respect to only one claim—that pertaining to backtested returns on portfolios containing REITs. In explaining his decision, the law judge stated: "Out of the four misrepresentations that the OIP alleges violate the Advisers Act, I find the [Respondents'] presentation's use and depiction of 'backtests' with REITs, by itself, misleading. Also, the sanction imposed would not change even if [I] were to find merit to the remaining allegations. I therefore do

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[7] *Id.* ¶¶ 23-25.

[8] *Id.* ¶¶ 26-27.

[9] *Id.* § III(A).

[10] *Id.* § IV.

[11] *E.g.*, Division's Post-Hearing Brief at 14-16 (inflation), 16-18 (REITs), 18-19 (fees), 19-21 (reallocation); Respondents' Post-Hearing Brief at 38-43 (inflation), 43-46 (REITs), 46-49 (fees), 49-52 (reallocation).

not make any findings as to the other three alleged misrepresentations."[12]

We have previously described the vital role that initial decisions play in the Commission's decisional process. "Unlike the law judge, we have not observed the parties and witnesses who appeared and testified at the . . . hearing. As the presiding officer at the hearing, the law judge is in the best position to make findings of fact, including credibility determinations, and resolve any conflicts in the evidence. Our review of the record cannot replace the law judge's personal experience with the witnesses."[13]

It is a matter of considerable importance, therefore, that initial decisions comply fully with Rule of Practice 360(b), which provides that such decisions "shall include[] findings and conclusions, and the reasons or basis therefor, as to *all* the *material* issues of fact, law or discretion *presented on the record* and the appropriate order, sanction, relief, or denial thereof."[14] Indeed, because the Advisers Act calibrates maximum civil penalties based upon a certain dollar amount for

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[12] Initial Decision, 2013 WL 3379719, at *2. The Initial Decision imposed a cease-and-desist order and a permanent associational bar, revoked Lucia's and RJLC's investment adviser registrations, and imposed civil penalties of $50,000 on Lucia and $250,000 on RJLC. *Id.* at *37-41. The Division of Enforcement had sought a greater civil penalty, but the law judge found the requested penalty to be excessive given the paucity of evidence of actual losses to investors, Respondents' otherwise clean regulatory record, and their cooperation with examiners. *Id.* at *41.

[13] *Nasdaq Stock Market, LLC*, Exchange Act Rel. No. 57741, 93 S.E.C. Docket 301, 2008 WL 1902073, at *1 (Apr. 30, 2008).

[14] 17 C.F.R. § 360(b) (emphases added). It bears noting, though, that Rule 360(b) does *not* require that law judges, in every instance, make specific findings as to every fact that the parties place in dispute or may consider pertinent.

"*each* act . . . or omission,"[15] and because we have repeatedly held that the determination of a proper sanction "rests on a careful consideration of each of the factors" enumerated in our precedent, "taking into account all of a respondent's arguments[]" and weighing the factors "against each other under the *specific facts and circumstances of each case,*"[16] the findings that a law judge makes in the course of disposing of all claims well might inform our determination of the appropriate sanction in the event of any appeal.[17] Moreover, even if no party chooses to seek review, the law judge's findings would assist our determination of whether to order review on own initiative pursuant to Rule of Practice 411(c).[18] Finally, we note that securing law judges' rulings on all claims presented for decision would facilitate the prompt resolution of administrative proceedings and avoid piecemeal litigation

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[15] 15 U.S.C. § 80b-3(i)(2) (emphasis added).

[16] *Impax Labs, Inc.*, Exchange Act Rel. No. 57864, 93 S.E.C. Docket 853, 2008 WL 2167956, at *11 (May 23, 2008); *see, e.g., John W. Lawton,* Advisers Act Rel. No. 3513, 2012 WL 6208750, at *9 n.42 (Dec. 13, 2012) ("sanctions determinations should show 'individual attention to the unique facts and circumstances of [the] case'"); *Janet Gurley Katz,* Exchange Act Rel. No. 61449, 97 S.E.C. Docket 2447, 2010 WL 358737 at *26 n.64 (Feb. 1, 2010) ("The appropriate sanction depends on the facts and circumstances of each particular case.") (quotation marks omitted).

[17] *Cf United States v. Fumo*, 655 F.3d 288, 311 (3d Cir. 2011) (holding, in the criminal sentencing context, that a "court should not refuse to find or calculate a loss" when doing so is necessary to determining the appropriate sentencing range under the Federal Sentencing Guidelines); *United States v. Robinson*, 435 F.3d 699, 701 (7th Cir. 2006) (similar).

[18] 17 C.F.R. § 201.411 (c); *see, e.g., Hunter Adams,* Exchange Act Rel. No. 52859, 86 S.E.C. Docket 1958, 2005 WL 3240600, at *1 & n.6 (Nov. 30, 2005); *Derek L. DuBois*, Securities Act Rel. No. 8264, Exchange Act Rel. No. 48332, 80 S.E.C. Docket 2403, 2003 WL 21946858, at *1, 5 (Aug. 13, 2003).

and appeals.[19] When claims are left unaddressed by an initial decision, and our subsequent review discerns error as to the resolution of the claims that were addressed, the law judge will have to spend additional time and effort on remand re-examining issues that could have been disposed of earlier.

The Initial Decision did not fully resolve the claims set forth in the OIP as to which the parties joined issue and then presented for decision. Accordingly, IT IS ORDERED that the matter be, and it hereby is, remanded to the law judge for issuance of an initial decision pursuant to Rule 360(b); and it is further ORDERED that the initial decision be filed with the Secretary of the Commission within 120 days from the date of this remand order.

By the Commission.

/s/
Elizabeth M. Murphy
Secretary

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[19] *Cf. Phifer v. Warden, U.S. Penitentiary, Terre Haute, Ind.*, 53 F.3d 859, 863 (7th Cir. 1995) (noting, in the *habeas corpus* context, that "[o]rdinarily, a district court should try to rule upon all of the grounds presented in a habeas petition," because "[g]ranting a writ but leaving claims unresolved fails to take the possibility of reversal on appeal into account; should an appellate court reverse the conditional grant of the writ, a petitioner's remaining claims will have to be addressed"); *Clisby v. Jones*, 960 F.2d 925, 936 (11th Cir. 1992) (en banc) (similar).

APPENDIX G

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 15-1345 **September Term, 2016**

SEC-3-15006

Filed On: February 16, 2017

Raymond J. Lucia Companies, Inc. and
Raymond J. Lucia,

Petitioners

v.

Securities and Exchange Commission,

Respondent

BEFORE: Garland*, Chief Judge; Henderson, Rogers, Tatel, Brown, Griffith, Kavanaugh, Srinivasan, Millett, Pillard, and Wilkins, Circuit Judges

ORDER

Upon consideration of petitioners' petition for rehearing en banc, the response thereto, and the vote in favor of the petition by a majority of judges eligible to participate, it is

*Chief Judge Garland did not participate in this matter.

ORDERED the petition be granted. Case No. 15-1345 will be reheard by the court sitting en banc. It is

FURTHER ORDERED that the judgment filed August 9, 2016 be vacated. It is

FURTHER ORDERED that oral argument before the en banc court be heard on Wednesday, May 24, 2017, in Courtroom # 20, Sixth Floor. It is

FURTHER ORDERED that, in addition to filing briefs electronically, the parties file 30 paper copies of each of their final briefs and the deferred appendix, in accordance with the following schedule:

Initial Brief for Petitioners	March 10, 2017
Initial Brief(s) for Amici Curiae	March 10, 2017
Initial Brief for Respondent	March 31, 2017
Initial Brief(s) for Amici Curiae, if any	March 31, 2017
Initial Reply Brief for Petitioners	April 10, 2017
Deferred Appendix	April 17, 2017
Final Briefs	April 24, 2017

The briefs are to be limited to the following issues:

1. Is the SEC administrative law judge who handled this case an inferior officer rather than an employee for the purposes of the Appointments Clause of Article II of the Constitution?

2. Should the court overrule *Landry v. FDIC*, 204 F.3d 1125 (D.C. Cir. 2000)?

Parties are directed to hand deliver the paper copies of their submissions to the Clerk's office by the

date due. To enhance the clarity of their briefs, the parties are urged to limit the use of abbreviations, including acronyms. While acronyms may be used for entities and statutes with widely recognized initials, briefs should not contain acronyms that are not widely known. *See D.C. Circuit Handbook of Practice and Internal Procedures* 41 (2017); Notice Regarding Use of Acronyms (D.C. Cir. Jan. 26, 2010).

Because the briefing schedule is keyed to the date of oral argument, the court will grant requests for extension of time limits only for extraordinarily compelling reasons. The briefs and appendix must contain the date the case is scheduled for oral argument at the top of the cover. *See* D.C. Cir. Rule 28(a)(8).

Separate order(s) will issue scheduling the time of oral argument and allocating oral argument time.

Per Curiam

FOR THE COURT:

Mark J. Langer, Clerk

BY: /s/
Michael C. McGrail
Deputy Clerk

APPENDIX H

U.S. Const. art. II, sec. 2

The President shall be Commander in Chief of the Army and Navy of the United States, and of the Militia of the several States, when called into the actual Service of the United States; he may require the Opinion, in writing, of the principal Officer in each of the executive Departments, upon any Subject relating to the Duties of their respective Offices, and he shall have Power to Grant Reprieves and Pardons for Offences against the United States, except in Cases of Impeachment.

He shall have Power, by and with the Advice and Consent of the Senate, to make Treaties, provided two thirds of the Senators present concur; and he shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

The President shall have Power to fill up all Vacancies that may happen during the Recess of the Senate, by granting Commissions which shall expire at the End of their next Session.

5 U.S.C. § 556. Hearings; presiding employees; powers and duties; burden of proof; evidence; record as basis of decision

(a) This section applies, according to the provisions thereof, to hearings required by section 553 or 554 of this title to be conducted in accordance with this section.

(b) There shall preside at the taking of evidence—

(1) the agency;

(2) one or more members of the body which comprises the agency; or

(3) one or more administrative law judges appointed under section 3105 of this title.

This subchapter does not supersede the conduct of specified classes of proceedings, in whole or in part, by or before boards or other employees specially provided for by or designated under statute. The functions of presiding employees and of employees participating in decisions in accordance with section 557 of this title shall be conducted in an impartial manner. A presiding or participating employee may at any time disqualify himself. On the filing in good faith of a timely and sufficient affidavit of personal bias or other disqualification of a presiding or participating employee, the agency shall determine the matter as a part of the record and decision in the case.

(c) Subject to published rules of the agency and within its powers, employees presiding at hearings may—

(1) administer oaths and affirmations;

(2) issue subpenas authorized by law;

(3) rule on offers of proof and receive relevant evidence;

(4) take depositions or have depositions taken when the ends of justice would be served;

(5) regulate the course of the hearing;

(6) hold conferences for the settlement or simplification of the issues by consent of the parties or by the use of alternative means of dispute resolution as provided in subchapter IV of this chapter;

(7) inform the parties as to the availability of one or more alternative means of dispute resolution, and encourage use of such methods;

(8) require the attendance at any conference held pursuant to paragraph (6) of at least one representative of each party who has authority to negotiate concerning resolution of issues in controversy;

(9) dispose of procedural requests or similar matters;

(10)make or recommend decisions in accordance with section 557 of this title; and

(11)take other action authorized by agency rule consistent with this subchapter.

(d) Except as otherwise provided by statute, the proponent of a rule or order has the burden of proof. Any oral or documentary evidence may be received, but the agency as a matter of policy shall provide for the exclusion of irrelevant, immaterial, or unduly repetitious evidence. A sanction may not be imposed or rule or order issued except on consideration of the whole record or those parts thereof cited by a party and supported by and in accordance with the reliable,

probative, and substantial evidence. The agency may, to the extent consistent with the interests of justice and the policy of the underlying statutes administered by the agency, consider a violation of section 557(d) of this title sufficient grounds for a decision adverse to a party who has knowingly committed such violation or knowingly caused such violation to occur. A party is entitled to present his case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts. In rule making or determining claims for money or benefits or applications for initial licenses an agency may, when a party will not be prejudiced thereby, adopt procedures for the submission of all or part of the evidence in written form.

(e) The transcript of testimony and exhibits, together with all papers and requests filed in the proceeding, constitutes the exclusive record for decision in accordance with section 557 of this title and, on payment of lawfully prescribed costs, shall be made available to the parties. When an agency decision rests on official notice of a material fact not appearing in the evidence in the record, a party is entitled, on timely request, to an opportunity to show the contrary.

5 U.S.C. § 557. Initial decisions; conclusiveness; review by agency; submissions by parties; contents of decisions; record

(a) This section applies, according to the provisions thereof, when a hearing is required to be conducted in accordance with section 556 of this title.

(b) When the agency did not preside at the reception of the evidence, the presiding employee or, in

cases not subject to section 554(d) of this title, an employee qualified to preside at hearings pursuant to section 556 of this title, shall initially decide the case unless the agency requires, either in specific cases or by general rule, the entire record to be certified to it for decision. When the presiding employee makes an initial decision, that decision then becomes the decision of the agency without further proceedings unless there is an appeal to, or review on motion of, the agency within time provided by rule. On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision except as it may limit the issues on notice or by rule. When the agency makes the decision without having presided at the reception of the evidence, the presiding employee or an employee qualified to preside at hearings pursuant to section 556 of this title shall first recommend a decision, except that in rule making or determining applications for initial licenses—

(1) instead thereof the agency may issue a tentative decision or one of its responsible employees may recommend a decision; or

(2) this procedure may be omitted in a case in which the agency finds on the record that due and timely execution of its functions imperatively and unavoidably so requires.

(c) Before a recommended, initial, or tentative decision, or a decision on agency review of the decision of subordinate employees, the parties are entitled to a reasonable opportunity to submit for the consideration of the employees participating in the decisions—

(1) proposed findings and conclusions; or

(2) exceptions to the decisions or recommended decisions of subordinate employees or to tentative agency decisions; and

(3) supporting reasons for the exceptions or proposed findings or conclusions.

The record shall show the ruling on each finding, conclusion, or exception presented. All decisions, including initial, recommended, and tentative decisions, are a part of the record and shall include a statement of—

(A) findings and conclusions, and the reasons or basis therefor, on all the material issues of fact, law, or discretion presented on the record; and

(B) the appropriate rule, order, sanction, relief, or denial thereof.

(d)(1) In any agency proceeding which is subject to subsection (a) of this section, except to the extent required for the disposition of ex parte matters as authorized by law—

(A) no interested person outside the agency shall make or knowingly cause to be made to any member of the body comprising the agency, administrative law judge, or other employee who is or may reasonably be expected to be involved in the decisional process of the proceeding, an ex parte communication relevant to the merits of the proceeding;

(B) no member of the body comprising the agency, administrative law judge, or other employee who is or may reasonably be expected to be involved in the decisional process of the proceeding, shall make or knowingly cause to be made to any interested person outside the agency an ex parte communication relevant to the merits of the proceeding;

(C) a member of the body comprising the agency, administrative law judge, or other employee who is or may reasonably be expected to be involved in the decisional process of such proceeding who receives, or who makes or knowingly causes to be made, a communication prohibited by this subsection shall place on the public record of the proceeding:

(i) all such written communications;

(ii) memoranda stating the substance of all such oral communications; and

(iii) all written responses, and memoranda stating the substance of all oral responses, to the materials described in clauses (i) and (ii) of this subparagraph;

(D) upon receipt of a communication knowingly made or knowingly caused to be made by a party in violation of this subsection, the agency, administrative law judge, or other employee presiding at the hearing may, to the extent consistent with the interests of justice and the policy of the underlying statutes, require the party to show cause why his claim or interest in the proceeding should not be dismissed, denied, disregarded, or otherwise adversely affected on account of such violation; and

(E) the prohibitions of this subsection shall apply beginning at such time as the agency may designate, but in no case shall they begin to apply later than the time at which a proceeding is noticed for hearing unless the person responsible for the communication has knowledge that it will be noticed, in which case the prohibitions shall apply beginning at the time of his acquisition of such knowledge.

(2) This subsection does not constitute authority to withhold information from Congress.

5 U.S.C. § 3105. Appointment of administrative law judges

Each agency shall appoint as many administrative law judges as are necessary for proceedings required to be conducted in accordance with sections 556 and 557 of this title. Administrative law judges shall be assigned to cases in rotation so far as practicable, and may not perform duties inconsistent with their duties and responsibilities as administrative law judges.

5 U.S.C. § 5372. Administrative law judges

(a) For the purposes of this section, the term "administrative law judge" means an administrative law judge appointed under section 3105.

(b)(1)(A) There shall be 3 levels of basic pay for administrative law judges (designated as AL–1, 2, and 3, respectively), and each such judge shall be paid at 1 of those levels, in accordance with the provisions of this section.

(B) Within level AL–3, there shall be 6 rates of basic pay, designated as AL–3, rates A through F, respectively. Level AL–2 and level AL–1 shall each have 1 rate of basic pay.

(C) The rate of basic pay for AL–3, rate A, may not be less than 65 percent of the rate of basic pay for level IV of the Executive Schedule, and the rate of basic pay for AL–1 may not exceed the rate for level IV of the Executive Schedule.

(2) The Office of Personnel Management shall determine, in accordance with procedures which the Office shall by regulation prescribe, the level in which each administrative-law-judge position shall be placed and the qualifications to be required for appointment to each level.

(3)(A) Upon appointment to a position in AL–3, an administrative law judge shall be paid at rate A of AL–3, and shall be advanced successively to rates B, C, and D of that level at the beginning of the next pay period following completion of 52 weeks of service in the next lower rate, and to rates E and F of that level at the beginning of the next pay period following completion of 104 weeks of service in the next lower rate.

(B) The Office of Personnel Management may provide for appointment of an administrative law judge in AL–3 at an advanced rate under such circumstances as the Office may determine appropriate.

(4) Subject to paragraph (1), effective at the beginning of the first applicable pay period commencing on or after the first day of the month in which an adjustment takes effect under section 5303 in the rates of basic pay under the General Schedule, each rate of basic pay for administrative law judges shall be adjusted by an amount determined by the President to be appropriate.

(c) The Office of Personnel Management shall prescribe regulations necessary to administer this section.

10 U.S.C. § 867. Art. 67. Review by the Court of Appeals for the Armed Forces

(a) The Court of Appeals for the Armed Forces shall review the record in—

(1) all cases in which the sentence, as affirmed by a Court of Criminal Appeals, extends to death;

(2) all cases reviewed by a Court of Criminal Appeals which the Judge Advocate General orders sent to the Court of Appeals for the Armed Forces for review; and

(3) all cases reviewed by a Court of Criminal Appeals in which, upon petition of the accused and on good cause shown, the Court of Appeals for the Armed Forces has granted a review.

(b) The accused may petition the Court of Appeals for the Armed Forces for review of a decision of a Court of Criminal Appeals within 60 days from the earlier of—

(1) the date on which the accused is notified of the decision of the Court of Criminal Appeals; or

(2) the date on which a copy of the decision of the Court of Criminal Appeals, after being served on appellate counsel of record for the accused (if any), is deposited in the United States mails for delivery by first-class certified mail to the accused at an address provided by the accused or, if no such address has been provided by the accused, at the latest address listed for the accused in his official service record.

The Court of Appeals for the Armed Forces shall act upon such a petition promptly in accordance with the rules of the court.

(c) In any case reviewed by it, the Court of Appeals for the Armed Forces may act only with respect to the findings and sentence as approved by the convening authority and as affirmed or set aside as incorrect in law by the Court of Criminal Appeals. In a case which the Judge Advocate General orders sent to the Court of Appeals for the Armed Forces, that action need be taken only with respect to the issues raised by him. In a case reviewed upon petition of the accused, that action need be taken only with respect to issues specified in the grant of review. The Court of Appeals for the Armed Forces shall take action only with respect to matters of law.

(d) If the Court of Appeals for the Armed Forces sets aside the findings and sentence, it may, except where the setting aside is based on lack of sufficient evidence in the record to support the findings, order a rehearing. If it sets aside the findings and sentence and does not order a rehearing, it shall order that the charges be dismissed.

(e) After it has acted on a case, the Court of Appeals for the Armed Forces may direct the Judge Advocate General to return the record to the Court of Criminal Appeals for further review in accordance with the decision of the court. Otherwise, unless there is to be further action by the President or the Secretary concerned, the Judge Advocate General shall instruct the convening authority to take action in accordance with that decision. If the court has ordered a rehearing, but the convening authority finds a rehearing impracticable, he may dismiss the charges.

15 U.S.C. § 77u. Hearings by Commission

All hearings shall be public and may be held before the Commission or an officer or officers of the Commission designated by it, and appropriate records thereof shall be kept.

15 U.S.C. § 78d–1. Delegation of functions by Commission

(a) Authorization; functions delegable; eligible persons; application of other laws

In addition to its existing authority, the Securities and Exchange Commission shall have the authority to delegate, by published order or rule, any of its functions to a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee board, including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter. Nothing in this section shall be deemed to supersede the provisions of section 556(b) of title 5, or to authorize the delegation of the function of rulemaking as defined in subchapter II of chapter 5 of title 5, with reference to general rules as distinguished from rules of particular applicability, or of the making of any rule pursuant to section 78s(c) of this title.

(b) Right of review; procedure

With respect to the delegation of any of its functions, as provided in subsection (a) of this section, the Commission shall retain a discretionary right to review the action of any such division of the Commission, individual Commissioner, administrative law judge, employee, or employee board, upon its own initiative or upon petition of a party to or intervenor in

such action, within such time and in such manner as the Commission by rule shall prescribe. The vote of one member of the Commission shall be sufficient to bring any such action before the Commission for review. A person or party shall be entitled to review by the Commission if he or it is adversely affected by action at a delegated level which (1) denies any request for action pursuant to section 77h(a) or section 77h(c) of this title or the first sentence of section 78*l*(d) of this title; (2) suspends trading in a security pursuant to section 78*l*(k) of this title; or (3) is pursuant to any provision of this chapter in a case of adjudication, as defined in section 551 of title 5, not required by this chapter to be determined on the record after notice and opportunity for hearing (except to the extent there is involved a matter described in section 554(a)(1) through (6) of such title 5).

(c) Finality of delegated action

If the right to exercise such review is declined, or if no such review is sought within the time stated in the rules promulgated by the Commission, then the action of any such division of the Commission, individual Commissioner, administrative law judge, employee, or employee board, shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission.

15 U.S.C. § 78v. Hearings by Commission

Hearings may be public and may be held before the Commission, any member or members thereof, or any officer or officers of the Commission designated by it, and appropriate records thereof shall be kept.

15 U.S.C. § 80a–40. Hearings by Commission

Hearings may be public and may be held before the Commission, any member or members thereof, or any officer or officers of the Commission designated by it, and appropriate records thereof shall be kept.

15 U.S.C. § 80b–12. Hearings

Hearings may be public and may be held before the Commission, any member or members thereof, or any officer or officers of the Commission designated by it, and appropriate records thereof shall be kept.

26 U.S.C. § 7443A. Special trial judges

(a) Appointment

The chief judge may, from time to time, appoint special trial judges who shall proceed under such rules and regulations as may be promulgated by the Tax Court.

(b) Proceedings which may be assigned to special trial judges

The chief judge may assign—

(1) any declaratory judgment proceeding,

(2) any proceeding under section 7463,

(3) any proceeding where neither the amount of the deficiency placed in dispute (within the meaning of section 7463) nor the amount of any claimed overpayment exceeds $10,000, and

(4) any other proceeding which the chief judge may designate,

to be heard by the special trial judges of the court.

(c) Authority to make court decision

The court may authorize a special trial judge to make the decision of the court with respect to any proceeding described in paragraph (1), (2), or (3) of subsection (b), subject to such conditions and review as the court may provide.

(d) Salary

Each special trial judge shall receive salary—

(1) at a rate equal to 90 percent of the rate for judges of the Tax Court, and

(2) in the same installments as such judges.

(e) Expenses for travel and subsistence

Subsection (d) of section 7443 shall apply to special trial judges subject to such rules and regulations as may be promulgated by the Tax Court.

ADMINISTRATIVE PROCEDURE ACT

[PUBLIC LAW 404—79TH CONGRESS]

[CHAPTER 324—2D SESSION]

[S. 7]

AN ACT To improve the administration of justice by prescribing fair administrative procedure

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

TITLE

SECTION 1. This Act may be cited as the "Administrative Procedure Act".

DEFINITIONS

SEC. 2. As used in this Act—

(a) AGENCY.—"Agency" means each authority (whether or not within or subject to review by another agency) of the Government of the United States other than Congress, the courts, or the governments of the possessions, Territories, or the District of Columbia. Nothing in this Act shall be construed to repeal delegations of authority as provided by law. Except as to the requirements of section 3, there shall be excluded from the operation of this Act (1) agencies composed of representatives of the parties or of representatives of organizations of the parties to the disputes determined by them, (2) courts martial and military commissions, (3) military or naval authority exercised in the field in time of war or in occupied territory, or (4) functions which by law expire on the termination of present hostilities, within any fixed period thereafter, or before July 1, 1947, and the functions conferred by the following statutes: Selective Training and Service Act of 1940; Contract Settlement Act of 1944; Surplus Property Act of 1944.

(b) PERSON AND PARTY.—"Person" includes individuals, partnerships, corporations, associations, or public or private organizations of any character other than agencies. "Party" includes any person or agency named or admitted as a party, or properly seeking and entitled as of right to be admitted as a party, in any

agency proceeding; but nothing herein shall be construed to prevent an agency from admitting any person or agency as a party for limited purposes.

(c) RULE AND RULE MAKING.—"Rule" means the whole or any part of any agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or to describe the organization, procedure, or practice requirements of any agency and includes the approval or prescription for the future of rates, wages, corporate or financial structures or reorganizations thereof, prices, facilities, appliances, services or allowances therefor or of valuations, costs, or accounting, or practices bearing upon any of the foregoing. "Rule making" means agency process for the formulation, amendment, or repeal of a rule.

(d) ORDER AND ADJUDICATION.—"Order" means the whole, or any part of the final disposition (whether affirmative, negative, injunctive, or declaratory in form) of any agency in any matter other than rule making but including licensing. "Adjudication" means agency process for the formulation of an order.

(e) LICENSE AND LICENSING.—"License" includes the whole or part of any agency permit, certificate, approval, registration, charter, membership, statutory exemption or other form of permission. "Licensing" includes agency process respecting the grant, renewal, denial, revocation, suspension, annulment, withdrawal, limitation amendment, modification, or conditioning of a license.

(f) SANCTION AND RELIEF.—"Sanction" includes the whole or part of any agency (1) prohibition, requirement, limitation, or other condition affecting the free-

dom of any person; (2) withholding of relief; (3) imposition of any form of penalty or fine; (4) destruction, taking, seizure, or withholding of property ; (5) assessment of damages, reimbursement, restitution, compensation, costs, charges, or fees; (6) requirement, revocation, or suspension of a license; or (7) taking of other compulsory or restrictive action. "Relief" includes the whole or part of any agency (1) grant of money, assistance, license, authority, exemption, exception, privilege, or remedy; (2) recognition of any claim, right, immunity, privilege, exemption, or exception; or (3) taking of any other action upon the application or petition of, and beneficial to, any person.

(g) AGENCY PROCEEDING AND ACTION.—"Agency proceeding" means any agency process as defined in subsections (c), (d), and (e) of this section. "Agency action" includes the whole or part of every agency rule, order, license, sanction, relief, or the equivalent or denial thereof, or failure to act.

PUBLIC INFORMATION

SEC. 3. Except to the extent that there is involved (1) any function of the United States requiring secrecy in the public interest or (2) any matter relating solely to the internal management of any agency—

(a) RULES.—Every agency shall separately state and currently publish in the Federal Register (1) descriptions of its central and field organization including delegations by the agency of final authority and the established places at which, and methods whereby, the public may secure information or make submittals or requests; (2) statements of the general course and method by which its functions are chan-

neled and determined, including the nature and requirements of all formal or informal procedures available as well as forms and instructions as to the scope and contents of all papers, reports, or examinations; and (3) substantive rules adopted as authorized by law and statements of general policy or interpretations formulated and adopted by the agency for the guidance of the public, but not rules addressed to and served upon named persons in accordance with law. No person shall in any manner be required to resort to organization or procedure not so published.

(b) OPINIONS AND ORDERS.—Every agency shall publish or, in accordance with published rule, make available to public inspection all final opinions or orders in the adjudication of cases (except those required for good cause to be held confidential and not cited as precedents) and all rules.

(c) PUBLIC RECORDS.—Save as otherwise required by statute, matters of official record shall in accordance with published rule be made available to persons properly and directly concerned except information held confidential for good cause found.

RULE MAKING

SEC. 4. Except to the extent that there is involved (1) any military, naval, or foreign affairs function of the United States or (2) any matter relating to agency management or personnel or to public property, loans, grants, benefits, or contracts—

(a) NOTICE.—General notice of proposed rule making shall be published in the Federal Register (unless all persons subject thereto are named and either personally served or otherwise have actual notice thereof

in accordance with law) and shall include (1) a statement of the time, place, and nature of public rule making proceedings; (2) reference to the authority under which the rule is proposed; and (3) either the terms or substance of the proposed rule or a description of the subjects and issues involved. Except where notice or hearing is required by statute, this subsection shall not apply to interpretative rules, general statements of policy, rules of agency organization, procedure, or practice, or in any situation in which the agency for good cause finds (and incorporates the finding and a brief statement of the reasons therefor in the rules issued) that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest.

(b) PROCEDURES.—After notice required by this section, the agency shall afford interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments with or without opportunity to present the same orally in any manner; and, after consideration of all relevant matter presented, the agency shall incorporate in any rules adopted a concise general statement of their basis and purpose. Where rules are required by statute to be made on the record after opportunity for an agency hearing, the requirements of sections 7 and 8 shall apply in place of the provisions of this subsection.

(c) EFFECTIVE DATES.—The required publication or service of any substantive rule (other than one granting or recognizing exemption or relieving restriction or interpretative rules and statements of policy) shall be made not less than thirty days prior to the effective date thereof except as otherwise provided

by the agency upon good cause found and published with the rule.

(d) PETITIONS.—Every agency shall accord any interested person the right to petition for the issuance, amendment, or repeal of a rule.

ADJUDICATION

SEC. 5. In every case of adjudication required by statute to be determined on the record after opportunity for an agency hearing, except to the extent that there is involved (1) any matter subject to a subsequent trial of the law and the facts de novo in any court; (2) the selection or tenure of an officer or employee of the United States other than examiners appointed pursuant to section 11; (3) proceedings in which decisions rest solely on inspections, tests, or elections; (4) the conduct of military, naval, or foreign affairs functions; (5) cases in which an agency is acting as an agent for a court; and (6) the certification of employee representatives—

(a) NOTICE.—Persons entitled to notice of an agency hearing shall be timely informed of (1) the time, place, and nature thereof; (2) the legal authority and jurisdiction under which the hearing is to be held; and (3) the matters of fact and law asserted. In instances in which private persons are the moving parties, other parties to the proceeding shall give prompt notice of issues controverted in fact or law; and in other instances agencies may by rule require responsive pleading. In fixing the times and places for hearings, due regard shall be had for the convenience and necessity of the parties or their representatives.

(b) PROCEDURE.—The agency shall afford all interested parties opportunity for (1) the submission and

consideration of facts, arguments, offers of settlement, or proposals of adjustment where time, the nature of the proceeding, and the public interest permit, and (2) to the extent that the parties are unable so to determine any controversy by consent, hearing, and decision upon notice and in conformity with sections 7 and 8.

(c) SEPARATION OF FUNCTIONS.—The same officers who preside at the reception of evidence pursuant to section 7 shall make the recommended decision or initial decision required by section 8 except where such officers become unavailable to the agency. Save to the extent required for the disposition of ex parte matters as authorized by law, no such officer shall consult any person or party on any fact in issue unless upon notice and opportunity for all parties to participate; nor shall such officer be responsible to or subject to the supervision or direction of any officer, employee, or agent engaged in the performance of investigative or prosecuting functions for any agency. No officer, employee, or agent engaged in the performance of investigative or prosecuting functions for any agency in any case shall, in that or a factually related case, participate or advise in the decision, recommended decision, or agency review pursuant to section 8 except as witness or counsel in public proceedings. This subsection shall not apply in determining applications for initial licenses or to proceedings involving the validity or application of rates, facilities, or practices of public utilities or carriers; nor shall it be applicable in any manner to the agency or any member or members of the body comprising the agency.

(d) DECLARATORY ORDERS.—The agency is authorized in its sound discretion, with like effect as in the

case of other orders, to issue a declaratory order to terminate a controversy or remove uncertainty.

ANCILLARY MATTERS

SEC 6. Except as otherwise provided in this Act—

(a) APPEARANCE.—Any person compelled to appear in person before any agency or representative thereof shall be accorded the right to be accompanied, represented, and advised by counsel or, if permitted by the agency, by other qualified representative. Every party shall be accorded the right to appear in person or by or with counsel or other duly qualified representative in any agency proceeding. So far as the orderly conduct of public business permits, any interested person may appear before any agency or its responsible officers or employees for the presentation, adjustment, or determination of any issue, request, or controversy in any proceeding (interlocutory, summary, or otherwise) or in connection with any agency function. Every agency shall proceed with reasonable dispatch to conclude any matter presented to it except that due regard shall be had for the convenience and necessity of the parties or their representatives. Nothing herein shall be construed either to grant or to deny to any person who is not a lawyer the right to appear for or represent others before any agency or in any agency proceeding.

(b) INVESTIGATIONS.—No process, requirement of a report, inspection, or other investigative act or demand shall be issued, made, or enforced in any manner or for any purpose except as authorized by law. Every person compelled to submit data or evidence shall be entitled to retain or, on payment of lawfully prescribed costs, procure a copy or transcript thereof,

except that in a nonpublic investigatory proceeding the witness may for good cause be limited to inspection of the official transcript of his testimony.

(c) SUBPENAS.—Agency subpenas authorized by law shall be issued to any party upon request and, as may be required by rules of procedure, upon a statement or showing of general relevance and reasonable scope of the evidence sought. Upon contest the court shall sustain any such subpena or similar process or demand to the extent that it is found to be in accordance with law and, in any proceeding for enforcement, shall issue an order requiring the appearance of the witness or the production of the evidence or data within a reasonable time under penalty of punishment for contempt in case of contumacious failure to comply.

(d) DENIALS.—Prompt notice shall be given of the denial in whole or in part of any written application, petition, or other request of any interested person made in connection with any agency proceeding. Except in affirming a prior denial or where the denial is self-explanatory, such notice shall be accompanied by a simple statement of procedural or other grounds.

HEARINGS

SEC. 7. In hearings which section 4 or 5 requires to be conducted pursuant to this section—

(a) PRESIDING OFFICERS.—There shall preside at the taking of evidence (1) the agency, (2) one or more members of the body which comprises the agency, or (3) one or more examiners appointed as provided in this Act; but nothing in this Act shall be deemed to supersede the conduct of specified classes of proceed-

ings in whole or part by or before boards or other officers specially provided for by or designated pursuant to statute. The functions of all presiding officers and of officers participating in decisions in conformity with section 8 shall be conducted in an impartial manner. Any such officer may at any time withdraw if he deems himself disqualified; and, upon the filing in good faith of a timely and sufficient affidavit of personal bias or disqualification of any such officer, the agency shall determine the matter as a part of the record and decision in the case.

(b) HEARING POWERS.—Officers presiding at hearings shall have authority, subject to the published rules of the agency and within its powers, to (1) administer oaths and affirmations, (2) issue subpenas authorized by law, (3) rule upon offers of proof and receive relevant evidence, (4) take or cause depositions to be taken whenever the ends of justice would be served thereby, (5) regulate the course of the hearing, (6) hold conferences for the settlement or simplification of the issues by consent of the parties, (7) dispose of procedural requests or similar matters, (8) make decisions or recommend decisions in conformity with section 8, and (9) take any other action authorized by agency rule consistent with this Act.

(c) EVIDENCE.—Except as statutes otherwise provide, the proponent of a rule or order shall have the burden of proof. Any oral or documentary evidence may be received, but every agency shall as a matter of policy provide for the exclusion of irrelevant, immaterial, or unduly repetitious evidence and no sanction shall be imposed or rule or order be issued except upon consideration of the whole record or such portions thereof as may be cited by any party and as supported by and in accordance with the reliable, probative, and

substantial evidence. Every party shall have the right to present his case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts. In rule making or determining claims for money or benefits or applications for initial licenses any agency may, where the interest of any party will not be prejudiced thereby, adopt procedures for the submission of all or part of the evidence in written form.

(d) RECORD.—The transcript of testimony and exhibits, together with all papers and requests filed in the proceeding, shall constitute the exclusive record for decision in accordance with section 8 and, upon payment of lawfully prescribed costs, shall be made available to the parties. Where any agency decision rests on official notice of a material fact not appearing in the evidence in the record, any party shall on timely request be afforded an opportunity to show the contrary.

DECISIONS

SEC. 8. In cases in which a hearing is required to be conducted in conformity with section 7—

(a) ACTION BY SUBORDINATES.—In cases in which the agency has not presided at the reception of the evidence, the officer who presided (or, in cases not subject to subsection (c) of section 5, any other officer or officers qualified to preside at hearings pursuant to section 7) shall initially decide the case or the agency shall require (in specific cases or by general rule) the entire record to be certified to it for initial decision. Whenever such officers make the initial decision and

in the absence of either an appeal to the agency or review upon motion of the agency within time provided by rule, such decision shall without further proceedings then become the decision of the agency. On appeal from or review of the initial decisions of such officers the agency shall, except as it may limit the issues upon notice or by rule, have all the powers which it would have in making the initial decision. Whenever the agency makes the initial decision without having presided at the reception of the evidence, such officers shall first recommend a decision except that in rule making or determining applications for initial licenses (1) in lieu thereof the agency may issue a tentative decision or any of its responsible officers may recommend a decision or (2) any such procedure may be omitted in any case in which the agency finds upon the record that due and timely execution of its functions imperatively and unavoidably so requires.

(b) SUBMITTALS AND DECISIONS.—Prior to each recommended, initial, or tentative decision, or decision upon agency review of the decision of subordinate officers the parties shall be afforded a reasonable opportunity to submit for the consideration of the officers participating in such decisions (1) proposed findings and conclusions, or (2) exceptions to the decisions or recommended decisions of subordinate officers or to tentative agency decisions, and (3) supporting reasons for findings or such exceptions or proposed findings or conclusions. The record shall show the ruling upon each such finding, conclusion, or exception presented. All decisions (including initial, recommended, or tentative decisions) shall become a part of the record and include a statement of (1) findings and conclusions, as well as the reasons or basis therefor, upon all the material issues of fact, law, or discretion presented on the

record; and (2) the appropriate rule, order, sanction, relief, or denial thereof.

SANCTIONS AND POWERS

SEC. 9. In the exercise of any power or authority—

(a) IN GENERAL.—No sanction shall be imposed or substantive rule or order be issued except within jurisdiction delegated to the agency and as authorized by law.

(b) LICENSES.—In any case in which application is made for a license required by law the agency, with due regard to the rights or privileges of all the interested parties or adversely affected persons and with reasonable dispatch, shall set and complete any proceedings required to be conducted pursuant to sections 7 and 8 of this Act or other proceedings required by law and shall make its decision. Except in cases of willfulness or those in which public health, interest or safety requires otherwise, no withdrawal, suspension, revocation, or annulment of any license shall be lawful unless, prior to the institution of agency proceedings therefor, facts or conduct which may warrant such action shall have been called to the attention of the licensee by the agency in writing and the licensee shall have been accorded opportunity to demonstrate or achieve compliance with all lawful requirements. In any case in which the licensee has, in accordance with agency rules, made timely and sufficient application for a renewal or a new license, no license with reference to any activity of a continuing nature shall expire until such application shall have been finally determined by the agency.

JUDICIAL REVIEW

SEC. 10. Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion—

(a) RIGHT OF REVIEW.—Any person suffering legal wrong because of any agency action, or adversely affected or aggrieved by such action within the meaning of any relevant statute, shall be entitled to judicial review thereof.

(b) FORM AND VENUE OR ACTION.—The form of proceeding for judicial review shall be any special statutory review proceeding relevant to the subject matter in any court specified by statute or, in the absence of inadequacy thereof, any applicable form of legal action (including actions for declaratory judgments or writs of prohibitory or mandatory injunction or habeas corpus) in any court of competent jurisdiction. Agency action shall be subject to judicial review in civil or criminal proceedings for judicial enforcement except to the extent that prior, adequate, and exclusive opportunity for such review is provided by law.

(c) REVIEWABLE ACTS.—Every agency action made reviewable by statute and every final agency action for which there is no other adequate remedy in any court shall be subject to judicial review. Any preliminary, procedural, or intermediate agency action or ruling not directly reviewable shall be subject to review upon the review of the final agency action. Except as otherwise expressly required by statute, agency action otherwise final shall be final for the purposes of this subsection whether or not there has been presented or determined any application for a declaratory order, for any form of reconsideration or (unless the agency

otherwise requires by rule and provides that the action meanwhile shall be inoperative) for an appeal to superior agency authority.

(d) INTERIM RELIEF.—Pending judicial review any agency is authorized, where it finds that justice so requires, to postpone the effective date of any action taken by it. Upon such conditions as may be required and to the extent necessary to prevent irreparable injury, every reviewing court (including every court to which a case may be taken on appeal from or upon application for certiorari or other writ to a reviewing court) is authorized to issue all necessary and appropriate process to postpone the effective date of any agency action or to preserve status or rights pending conclusion of the review proceedings.

(e) SCOPE OF REVIEW.—So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; (3) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 7 and 8 or otherwise reviewed on the record of an agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by

the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error.

EXAMINERS

SEC. 11. Subject to the civil-service and other laws to the extent not inconsistent with this Act, there shall be appointed by and for each agency as many qualified and competent examiners as may be necessary for proceedings pursuant to sections 7 and 8, who shall be assigned to cases in rotation so far as practicable and shall perform no duties inconsistent with their duties and responsibilities as examiners. Examiners shall be removable by the agency in which they are employed only for good cause established and determined by the Civil Service Commission (hereinafter called the Commission) after opportunity for hearing and upon the record thereof. Examiners shall receive compensation prescribed by the Commission independently of agency recommendations or ratings and in accordance with the Classification Act of 1923, as amended, except that the provisions of paragraphs (2) and (3) of subsection (b) of section 7 of said Act, as amended, and the provisions of section 9 of said Act, as amended, shall not be applicable. Agencies occasionally or temporarily insufficiently staffed may utilize examiners selected by the Commission from and with the consent of other agencies. For the purposes of this section, the Commission is authorized to make investigations, require reports by agencies, issue reports, including an annual report to the Congress, promulgate rules, appoint such advisory committees as may be deemed necessary, recommend legislation, subpena witnesses

or records, and pay witness fees as established for the United States courts.

CONSTRUCTION AND EFFECT

SEC. 12. Nothing in this Act shall be held to diminish the constitutional rights of any person or to limit or repeal additional requirements imposed by statute or otherwise recognized by law. Except as otherwise required by law, all requirements or privileges relating to evidence or procedure shall apply equally to agencies and persons. If any provision of this Act or the application thereof is held invalid, the remainder of this Act or other applications of such provision shall not be affected. Every agency is granted all authority necessary to comply with the requirements of this Act through the issuance of rules or otherwise. No subsequent legislation shall be held to supersede or modify the provisions of this Act except to the extent that such legislation shall do so expressly. This Act shall take effect three months after its approval except that sections 7 and 8 shall take effect six months after such approval, the requirement of the selection of examiners pursuant to section 11 shall not become effective until one year after such approval, and no procedural requirement shall be mandatory as to any agency proceeding initiated prior to the effective date of such requirement.

Approved June 11, 1946.

17 C.F.R. § 200.14 Office of Administrative Law Judges.

(a) Under the Administrative Procedure Act (5 U.S.C. 551–559) and the federal securities laws, the

Office of Administrative Law Judges conducts hearings in proceedings instituted by the Commission. The Administrative Law Judges are responsible for the fair and orderly conduct of the proceedings and have the authority to:

(1) Administer oaths and affirmations;

(2) Issue subpoenas;

(3) Rule on offers of proof;

(4) Examine witnesses;

(5) Regulate the course of a hearing;

(6) Hold pre-hearing conferences;

(7) Rule upon motions; and

(8) Unless waived by the parties, prepare an initial decision containing the conclusions as to the factual and legal issues presented, and issue an appropriate order.

(b) The Chief Administrative Law Judge performs the duties of an Administrative Law Judge under the Administrative Procedure Act and the duties delegated to him or her by the Commission that are compatible with those duties. The Chief Administrative Law Judge is responsible for the orderly functioning of the Office of Administrative Law Judges apart from the conduct of administrative proceedings and acts as liaison between that Office and the Commission.

17 C.F.R. § 201.110 Presiding officer.

All proceedings shall be presided over by the Commission or, if the Commission so orders, by a hearing

officer. When the Commission designates that the hearing officer shall be an administrative law judge, the Chief Administrative Law Judge shall select, pursuant to 17 CFR 200.30–10, the administrative law judge to preside.

17 C.F.R. § 201.111 Hearing officer: Authority.

The hearing officer shall have the authority to do all things necessary and appropriate to discharge his or her duties. No provision of these Rules of Practice shall be construed to limit the powers of the hearing officer provided by the Administrative Procedure Act, 5 U.S.C. 556, 557. The powers of the hearing officer include, but are not limited to, the following:

(a) Administering oaths and affirmations;

(b) Issuing subpoenas authorized by law and revoking, quashing, or modifying any such subpoena;

(c) Receiving relevant evidence and ruling upon the admission of evidence and offers of proof;

(d) Regulating the course of a proceeding and the conduct of the parties and their counsel;

(e) Holding prehearing and other conferences as set forth in § 201.221 and requiring the attendance at any such conference of at least one representative of each party who has authority to negotiate concerning the resolution of issues in controversy;

(f) Recusing himself or herself upon motion made by a party or upon his or her own motion;

(g) Ordering, in his or her discretion, in a proceeding involving more than one respondent, that the interested division indicate, on the record, at least one

day prior to the presentation of any evidence, each respondent against whom that evidence will be offered;

(h) Subject to any limitations set forth elsewhere in these Rules of Practice, considering and ruling upon all procedural and other motions, including a motion to correct a manifest error of fact in the initial decision. A motion to correct is properly filed under this Rule only if the basis for the motion is a patent misstatement of fact in the initial decision. Any motion to correct must be filed within ten days of the initial decision. A brief in opposition may be filed within five days of a motion to correct. The hearing officer shall have 20 days from the date of filing of any brief in opposition filed to rule on a motion to correct;

(i) Preparing an initial decision as provided in § 201.360;

(j) Upon notice to all parties, reopening any hearing prior to the filing of an initial decision therein, or, if no initial decision is to be filed, prior to the time fixed for the filing of final briefs with the Commission; and

(k) Informing the parties as to the availability of one or more alternative means of dispute resolution, and encouraging the use of such methods.

17 C.F.R. § 201.155 Default; motion to set aside default.

(a) A party to a proceeding may be deemed to be in default and the Commission or the hearing officer may determine the proceeding against that party upon consideration of the record, including the order

instituting proceedings, the allegations of which may be deemed to be true, if that party fails:

(1) To appear, in person or through a representative, at a hearing or conference of which that party has been notified;

(2) To answer, to respond to a dispositive motion within the time provided, or otherwise to defend the proceeding; or

(3) To cure a deficient filing within the time specified by the commission or the hearing officer pursuant to § 201.180(b).

(b) A motion to set aside a default shall be made within a reasonable time, state the reasons for the failure to appear or defend, and specify the nature of the proposed defense in the proceeding. In order to prevent injustice and on such conditions as may be appropriate, the hearing officer, at any time prior to the filing of the initial decision, or the Commission, at any time, may for good cause shown set aside a default.

17 C.F.R. § 201.180 Sanctions.

(a) *Contemptuous conduct*—(1) *Subject to exclusion or suspension.* Contemptuous conduct by any person before the Commission or a hearing officer during any proceeding, including any conference, shall be grounds for the Commission or the hearing officer to:

(i) Exclude that person from such hearing or conference, or any portion thereof; and/or

(ii) Summarily suspend that person from representing others in the proceeding in which such conduct occurred for the duration, or any portion, of the proceeding.

(2) *Review procedure.* A person excluded from a hearing or conference, or a counsel summarily suspended from practice for the duration or any portion of a proceeding, may seek review of the exclusion or suspension by filing with the Commission, within three days of the exclusion or suspension order, a motion to vacate the order. The Commission shall consider such motion on an expedited basis as provided in § 201.500.

(3) *Adjournment.* Upon motion by a party represented by counsel subject to an order of exclusion or suspension, an adjournment shall be granted to allow the retention of new counsel. In determining the length of an adjournment, the Commission or hearing officer shall consider, in addition to the factors set forth in § 201.161, the availability of co-counsel for the party or of other members of a suspended counsel's firm.

(b) *Deficient filings; leave to cure deficiencies.* The Commission or the hearing officer may reject, in whole or in part, any filing that fails to comply with any requirements of these Rules of Practice or of any order issued in the proceeding in which the filing was made. Any such filings shall not be part of the record. The Commission or the hearing officer may direct a party to cure any deficiencies and to resubmit the filing within a fixed time period.

(c) *Failure to make required filing or to cure deficient filing.* The Commission or the hearing officer

may enter a default pursuant to § 201.155, dismiss the case, decide the particular matter at issue against that person, or prohibit the introduction of evidence or exclude testimony concerning that matter if a person fails:

(1) To make a filing required under these Rules of Practice; or

(2) To cure a deficient filing within the time specified by the Commission or the hearing officer pursuant to paragraph (b) of this section.

17 C.F.R. § 201.232 Subpoenas.

(a) *Availability; procedure.* In connection with any hearing ordered by the Commission, a party may request the issuance of subpoenas requiring the attendance and testimony of witnesses at the designated time and place of hearing, and subpoenas requiring the production of documentary or other tangible evidence returnable at any designated time or place. Unless made on the record at a hearing, requests for issuance of a subpoena shall be made in writing and served on each party pursuant to § 201.150. A person whose request for a subpoena has been denied or modified may not request that any other person issue the subpoena.

(1) *Unavailability of hearing officer.* In the event that the hearing officer assigned to a proceeding is unavailable, the party seeking issuance of the subpoena may seek its issuance from the first available of the following persons: The Chief Administrative Law Judge, the law judge most senior in service as a law judge, the duty officer, any other member of the Com-

mission, or any other person designated by the Commission to issue subpoenas. Requests for issuance of a subpoena made to the Commission, or any member thereof, must be submitted to the Secretary, not to an individual Commissioner.

(2) *Signing may be delegated.* A hearing officer may authorize issuance of a subpoena, and may delegate the manual signing of the subpoena to any other person authorized to issue subpoenas.

(b) *Standards for issuance.* Where it appears to the person asked to issue the subpoena that the subpoena sought may be unreasonable, oppressive, excessive in scope, or unduly burdensome, he or she may, in his or her discretion, as a condition precedent to the issuance of the subpoena, require the person seeking the subpoena to show the general relevance and reasonable scope of the testimony or other evidence sought. If after consideration of all the circumstances, the person requested to issue the subpoena determines that the subpoena or any of its terms is unreasonable, oppressive, excessive in scope, or unduly burdensome, he or she may refuse to issue the subpoena, or issue it only upon such conditions as fairness requires. In making the foregoing determination, the person issuing the subpoena may inquire of the other participants whether they will stipulate to the facts sought to be proved.

(c) *Service.* Service shall be made pursuant to the provisions of § 201.150 (b) through (d). The provisions of this paragraph (c) shall apply to the issuance of subpoenas for purposes of investigations, as required by 17 CFR 203.8, as well as hearings.

(d) *Tender of fees required.* When a subpoena compelling the attendance of a person at a hearing or

deposition is issued at the instance of anyone other than an officer or agency of the United States, service is valid only if the subpoena is accompanied by a tender to the subpoenaed person of the fees for one day's attendance and mileage specified by paragraph (f) of this section.

(e) *Application to quash or modify.* (1) Any person to whom a subpoena is directed, or who is an owner, creator or the subject of the documents that are to be produced pursuant to a subpoena, or any party may, prior to the time specified therein for compliance, but in no event more than 15 days after the date of service of such subpoena, request that the subpoena be quashed or modified. Such request shall be made by application filed with the Secretary and served on all parties pursuant to § 201.150. The party on whose behalf the subpoena was issued may, within five days of service of the application, file an opposition to the application. If a hearing officer has been assigned to the proceeding, the application to quash shall be directed to that hearing officer for consideration, even if the subpoena was issued by another person.

(2) *Standards governing application to quash or modify.* If compliance with the subpoena would be unreasonable, oppressive or unduly burdensome, the hearing officer or the Commission shall quash or modify the subpoena, or may order return of the subpoena only upon specified conditions. These conditions may include but are not limited to a requirement that the party on whose behalf the subpoena was issued shall make reasonable compensation to the person to whom the subpoena was addressed for the cost of copying or transporting evidence to the place for return of the subpoena.

(f) *Witness fees and mileage.* Witnesses summoned before the Commission shall be paid the same fees and mileage that are paid to witnesses in the courts of the United States, and witnesses whose depositions are taken and the persons taking the same shall severally be entitled to the same fees as are paid for like services in the courts of the United States. Witness fees and mileage shall be paid by the party at whose instance the witnesses appear.

17 C.F.R. § 201.360 Initial decision of hearing officer.

(a)(1) *When required.* Unless the Commission directs otherwise, the hearing officer shall prepare an initial decision in any proceeding in which the Commission directs a hearing officer to preside at a hearing, provided, however, that an initial decision may be waived by the parties with the consent of the hearing officer pursuant to § 201.202.

(2) *Time period for filing initial decision.* In the order instituting proceedings, the Commission will specify a time period in which the hearing officer's initial decision must be filed with the Secretary. In the Commission's discretion, after consideration of the nature, complexity, and urgency of the subject matter, and with due regard for the public interest and the protection of investors, this time period will be either 120, 210 or 300 days from the date of service of the order. Under the 300-day timeline, the hearing officer shall issue an order providing that there shall be approximately 4 months from the order instituting the proceeding to the hearing, approximately 2 months for the parties to obtain the transcript and submit briefs, and approximately 4 months after briefing for the

hearing officer to issue an initial decision. Under the 210-day timeline, the hearing officer shall issue an order providing that there shall be approximately 2 ½ months from the order instituting the proceeding to the hearing, approximately 2 months for the parties to review the transcript and submit briefs, and approximately 2 ½ months after briefing for the hearing officer to issue an initial decision. Under the 120-day timeline, the hearing officer shall issue an order providing that there shall be approximately 1 month from the order instituting the proceeding to the hearing, approximately 2 months for the parties to review the transcript and submit briefs, and approximately 1 month after briefing for the hearing officer to issue an initial decision. These deadlines confer no substantive rights on respondents. If a stay is granted pursuant to § 201.210(c)(3), the time period specified in the order instituting proceedings in which the hearing officer's initial decision must be filed with the Secretary, as well as any other time limits established in orders issued by the hearing officer in the proceeding, shall be automatically tolled during the period while the stay is in effect.

(3) *Motion for extension.* In the event that the hearing officer presiding over the proceeding determines that it will not be possible to issue the initial decision within the specified period of time, the hearing officer should consult with the Chief Administrative Law Judge. Following such consultation, the Chief Administrative Law Judge may determine, in his or her discretion, to submit a motion to the Commission requesting an extension of the time period for filing the initial decision. This motion must be filed no later than 30 days prior to the expiration of the time specified in the order for issuance of an initial decision. The motion will be served upon all parties in the

proceeding, who may file with the Commission statements in support of or in opposition to the motion. If the Commission determines that additional time is necessary or appropriate in the public interest, the Commission shall issue an order extending the time period for filing the initial decision.

(b) *Content.* An initial decision shall include: Findings and conclusions, and the reasons or basis therefor, as to all the material issues of fact, law or discretion presented on the record and the appropriate order, sanction, relief, or denial thereof. The initial decision shall also state the time period, not to exceed 21 days after service of the decision, except for good cause shown, within which a petition for review of the initial decision may be filed. The reasons for any extension of time shall be stated in the initial decision. The initial decision shall also include a statement that, as provided in paragraph (d) of this section:

(1) The Commission will enter an order of finality as to each party unless a party or an aggrieved person entitled to review timely files a petition for review of the initial decision or a motion to correct a manifest error of fact in the initial decision with the hearing officer, or the Commission determines on its own initiative to review the initial decision; and

(2) If a party or an aggrieved person entitled to review timely files a petition for review or a motion to correct a manifest error of fact in the initial decision with the hearing officer, or if the Commission takes action to review as to a party or an aggrieved person entitled to review, the initial decision shall not become final as to that party or person.

(c) *Filing, service and publication.* The hearing officer shall file the initial decision with the Secretary.

The Secretary shall promptly serve the initial decision upon the parties and shall promptly publish notice of the filing thereof in the *SEC News Digest.* Thereafter, the Secretary shall publish the initial decision in the *SEC Docket*; provided, however, that in nonpublic proceedings no notice shall be published unless the Commission otherwise directs.

(d) *Finality.* (1) If a party or an aggrieved person entitled to review timely files a petition for review or a motion to correct a manifest error of fact in the initial decision, or if the Commission on its own initiative orders review of a decision with respect to a party or a person aggrieved who would be entitled to review, the initial decision shall not become final as to that party or person.

(2) If a party or aggrieved person entitled to review fails to file timely a petition for review or a motion to correct a manifest error of fact in the initial decision, and if the Commission does not order review of a decision on its own initiative, the Commission will issue an order that the decision has become final as to that party. The decision becomes final upon issuance of the order. The order of finality shall state the date on which sanctions, if any, take effect. Notice of the order shall be published in the *SEC Docket* and on the SEC Web site.

17 C.F.R. § 201.410 Appeal of initial decisions by hearing officers.

(a) *Petition for review; when available.* In any proceeding in which an initial decision is made by a hearing officer, any party, and any other person who would have been entitled to judicial review of the decision entered therein if the Commission itself had

made the decision, may file a petition for review of the decision with the Commission.

(b) *Procedure.* The petition for review of an initial decision shall be filed with the Commission within such time after service of the initial decision as prescribed by the hearing officer pursuant to § 201.360(b) unless a party has filed a motion to correct an initial decision with the hearing officer. If such correction has been sought, a party shall have 21 days from the date of the hearing officer's order resolving the motion to correct to file a petition for review. The petition shall set forth the specific findings and conclusions of the initial decision as to which exception is taken, together with supporting reasons for each exception. Supporting reasons may be stated in summary form. Any exception to an initial decision not stated in the petition for review, or in a previously filed proposed finding made pursuant to § 201.340 may, at the discretion of the Commission, be deemed to have been waived by the petitioner. In the event a petition for review is filed, any other party to the proceeding may file a cross-petition for review within the original time allowed for seeking review or within ten days from the date that the petition for review was filed, whichever is later.

(c) *Financial disclosure statement requirement.* Any person who files a petition for review of an initial decision that asserts that person's inability to pay either disgorgement, interest or a penalty shall file with the opening brief a sworn financial disclosure statement containing the information specified in § 201.630(b).

(d) [Reserved]

(e) *Prerequisite to judicial review.* Pursuant to Section 704 of the Administrative Procedure Act, 5 U.S.C. 704, a petition to the Commission for review of an initial decision is a prerequisite to the seeking of judicial review of a final order entered pursuant to such decision.

17 C.F.R. § 201.411 Commission consideration of initial decisions by hearing officers.

(a) *Scope of review.* The Commission may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part, an initial decision by a hearing officer and may make any findings or conclusions that in its judgment are proper and on the basis of the record.

(b) *Standards for granting review pursuant to a petition for review*—(1) *Mandatory review.* After a petition for review has been filed, the Commission shall review any initial decision that:

(i) Denies any request for action pursuant to Section 8(a) or Section 8(c) of the Securities Act of 1933, 15 U.S.C. 77h(a), (c), or the first sentence of Section 12(d) of the Exchange Act, 15 U.S.C. 78*l*(d);

(ii) Suspends trading in a security pursuant to Section 12(k) of the Exchange Act, 15 U.S.C. 78l(k); or

(iii) Is in a case of adjudication (as defined in 5 U.S.C. 551) not required to be determined on the record after notice and opportunity for hearing (except to the extent there is involved a matter described in 5 U.S.C. 554(a) (1) through (6)).

(2) *Discretionary review.* The Commission may decline to review any other decision. In determining

whether to grant review, the Commission shall consider whether the petition for review makes a reasonable showing that:

(i) A prejudicial error was committed in the conduct of the proceeding; or

(ii) The decision embodies:

(A) A finding or conclusion of material fact that is clearly erroneous; or

(B) A conclusion of law that is erroneous; or

(C) An exercise of discretion or decision of law or policy that is important and that the Commission should review.

(c) *Commission review other than pursuant to a petition for review.* The Commission may, on its own initiative, order review of any initial decision, or any portion of any initial decision, within 21 days after the end of the period established for filing a petition for review pursuant to § 210.410(b). A party who does not intend to file a petition for review, and who desires the Commission's determination whether to order review on its own initiative to be made in a shorter time, may make a motion for an expedited decision, accompanied by a written statement that the party waives its right to file a petition for review. The vote of one member of the Commission, conveyed to the Secretary, shall be sufficient to bring a matter before the Commission for review.

(d) *Limitations on matters reviewed.* Review by the Commission of an initial decision shall be limited to the issues specified in the petition for review or the issues, if any, specified in the briefing schedule order issued pursuant to § 201.450(a). On notice to all parties, however, the Commission may, at any time prior

to issuance of its decision, raise and determine any other matters that it deems material, with opportunity for oral or written argument thereon by the parties.

(e) *Summary affirmance.* (1) At any time within 21 days after the filing of a petition for review pursuant to § 201.410(b), any party may file a motion in accordance with § 201.154 asking that the Commission summarily affirm an initial decision. Any party may file an opposition and reply to such motion in accordance with § 201.154. Pending determination of the motion for summary affirmance, the Commission, in its discretion, may delay issuance of a briefing schedule order pursuant to § 201.450.

(2) Upon consideration of the motion and any opposition or upon its own initiative, the Commission may summarily affirm an initial decision. The Commission may grant summary affirmance if it finds that no issue raised in the initial decision warrants consideration by the Commission of further oral or written argument. The Commission will decline to grant summary affirmance upon a reasonable showing that a prejudicial error was committed in the conduct of the proceeding or that the decision embodies an exercise of discretion or decision of law or policy that is important and that the Commission should review.

(f) *Failure to obtain a majority.* In the event a majority of participating Commissioners do not agree to a disposition on the merits, the initial decision shall be of no effect, and an order will be issued in accordance with this result.

APPENDIX I

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-15519

In the Matter of	:
Timbervest, LLC,	:
Joel Barth Shapiro,	:
Walter William Anthony Boden, III,	:
Donald David Zell, Jr.,	:
and Gordon Jones II,	:
Respondents.	:

NOTICE OF FILING

On May 27, 2015, the Commission ordered the Division of Enforcement ("Division") to file and serve on Respondents by June 4, 2015, an affidavit and any supporting materials "setting forth the manner in which administrative law judge ("ALJ") Cameron Elliot and Chief ALJ Brenda Murray were hired, including the method of selection and appointment." The Division hereby submits the attached Affidavit, which contains the factual information the Division believes legally relevant to resolving Respondents' Article II-based constitutional claims—namely that, consistent with his status as an agency employee and not a constitutional officer, ALJ Elliot was not hired through a

process involving the approval of the individual members of the Commission.[1]

The Division also submits the following background information regarding the selection and hiring of Commission ALJs: Pursuant to current statutes and regulations, the hiring process for Commission ALJs is overseen by the U.S. Office of Personnel Management ("OPM"), which administers the competitive examination for selecting all ALJs across the federal government. *See* 5 U.S.C. §§ 1104, 1302; 5 C.F.R. § 930.201(d)-(e). As do other agencies, the Commission hires its ALJs through this OPM process. *See* 5 U.S.C. § 3105; 5 C.F.R. § 930.201(f). When the Commission seeks to hire a new ALJ, Chief ALJ Murray obtains from OPM a list of eligible candidates; a selection is made from the top three candidates on that list. *See* 5 U.S.C. §§ 3317, 3318; 5 C.F.R. §§ 332.402, 332.404, 930.204(a). Chief ALJ Murray and an interview committee then make a preliminary selection from among the available candidates. Their recommendation is

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[1] Respondents' contention that ALJ Elliot's hiring violated the Appointments Clause rests on the false premise that he is an inferior constitutional officer. As the Division has explained (Memorandum of Law in Response to the Commission's Order Requesting Supplemental Briefing at 4-13), ALJ Elliot is an employee, not an inferior officer. To the extent the Commission disagrees with the Division on this point, the Division believes that the facts set forth in the affidavit—*i.e.*, facts relating to ALJ Elliot's hiring—are sufficient for the Commission's consideration of Respondents' Appointments Clause challenge. Further, the Division notes that it was limited in its ability to collect information regarding ALJ hiring in light of *ex parte* considerations related to pending litigation.

subject to final approval and processing by the Commission's Office of Human Resources.[2]

It is the Division's understanding that the above process was employed as to ALJ Elliot, who began work at the agency in 2011. As for earlier hires, it is likely the Commission employed a similar, if not identical, hiring process. But the Division acknowledges that it is possible that internal processes have shifted over time with changing laws and circumstances, and thus the hiring process may have been somewhat different with respect to previously hired ALJs. For instance, Chief ALJ Murray began work at the agency in 1988 and information regarding hiring practices at that time is not readily accessible.

This 4th day of June, 2015

Respectfully submitted,

/s/ M. Graham Loomis

M. Graham Loomis
Robert K. Gordon
Anthony J. Winter
Attorneys for Division of Enforcement
Securities and Exchange Commission
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Atlanta, Georgia 30326-1232

* * *

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[2] OPM retains oversight over each agency's "decisions concerning the appointment, pay, and tenure" of ALJs, 5 C.F.R. § 930.201(e)(2), and establishes classification and qualification standards for ALJ positions, *id.* § 930.201(e)(3). ALJs also are paid according to a statutorily prescribed pay schedule. 5 U.S.C. § 5372; 5 C.F.R. §§ 930.205, 206; *see also* http://www.opm.gov/policy-data-oversight/pay-leave/pay-administration/fact-sheets/administrative-law-judge-pay-system/ (ALJ pay system).

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-15519

In the Matter of	:
	:
Timbervest, LLC,	:
Joel Barth Shapiro,	:
Walter William Anthony Boden, III,	:
Donald David Zell, Jr.,	:
and Gordon Jones II,	:
	:
Respondents.	:

AFFIDAVIT OF JAYNE L. SEIDMAN

Jayne L. Seidman, states that:

1. I am a Senior Officer at the Commission and Deputy Chief Operating Officer.

2. I make this Affidavit in response to the Commission's May 27, 2015, Order Requesting Additional Submissions and Additional Briefing.

3. In its May 27, 2015, Order, the Commission directed the Division to file and serve on Respondents by June 4, 2015, an affidavit and any supporting materials "setting forth the manner in which ALJ Cameron Elliot and Chief ALJ Brenda Murray were hired, including the method of selection and appointment."

4. Based on my knowledge of the Commission's ALJ hiring process, ALJ Elliot was not hired through

a process involving the approval of the individual members of the Commission.

I declare under penalty of perjury that the foregoing is true and correct.

Executed on 4th day of June, 2015.

s/
Jayne L. Seidman
Deputy Chief Operating Officer

APPENDIX J

CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES

Pursuant to Circuit Rule 28, Petitioners Raymond J. Lucia Companies, Inc., and Raymond J. Lucia (collectively, "petitioners"), respectfully submit this Certificate as to Parties, Rulings, and Related Cases:

* * *

C. Related Cases

This matter has not previously been before this Court. Counsel for petitioners are not aware of any related cases currently pending in this Court or in any other court within the meaning of Circuit Rule 28(a)(1)(C).

Counsel for petitioners note, however, that the constitutionality of the method of appointment of the Commission's Administrative Law Judges has been raised in a number of other active proceedings in courts around the country, including the following:

- *Tilton v. SEC*, No. 16-906 (S. Ct.)
- *Timbervest, LLC v. SEC*, No. 15-1416 (D.C. Cir.)
- *Riad v. SEC*, No. 16-1275 (D.C. Cir.)
- *Bennett v. SEC*, No. 16-3827 (8th Cir.)
- *Aesoph v. SEC*, No. 16-3830 (8th Cir.) (consolidated with *Bennett*, No. 16- 3827, *supra*)
- *Feathers v. SEC*, No. 15-70102 (9th Cir.)
- *J.S. Oliver Capital Management v. SEC*, No. 16-72703 (9th Cir.)

- *Bandimere v. SEC*, No. 19-9586 (10th Cir.)
- *Imperato v. SEC*, No. 15-11574 (11th Cir.)
- *RD Legal Capital LLC v. SEC*, No. 16-5104 (D.N.J.)

In addition, the following proceedings open before the Commission according to its website were previously identified by either petitioners or the Commission as involving the same constitutional issue:

- *In the Matter of Laurie Bebo & John Buono, CPA*, File No. 3-16293
- *In the Matter of Bennett Group Financial Services, LLC & Dawn J. Bennett*, File No. 3-16801
- *In the Matter of Gregory T. Bolan, Jr.*, File No. 3-16178
- *In the Matter of Frank H. Chiappone, et al.*, File No. 3-15514
- *In the Matter of Edward M. Daspin, et al.*, File No. 3-16509
- *In the Matter of Gilles T. De Charsonville*, File No. 3-16712
- *In the Matter of Barbara Duka*, File No. 3-16349
- *In the Matter of Equity Trust Company*, File No. 3-16594
- *In the Matter of Gray Financial Group, Inc., et al.*, File No. 3-16554
- *In the Matter of Harding Advisory LLC & Wing F. Chau*, File No. 3-15574
- *In the Matter of Charles L. Hill, Jr.*, File No. 3-16383
- *In the Matter of Ironridge Global Partners, LLC & Ironridge Global IV, Ltd.*, File No. 3-16649

- *In the Matter of John Thomas Capital Management Group LLC d/b/a Patriot28, & George R. Jarkesy, Jr.*, File No. 3-15255
- *In the Matter of J.S. Oliver Capital Management, L.P., & Ian O. Mausner*, File No. 3-15446
- *In the Matter of Lawrence M. Labine*, File No. 3-15967
- *In the Matter of Paul Edward "Ed" Lloyd, Jr., CPA*, File No. 3-16182
- *In the Matter of Natural Blue Resources, Inc., et al.*, File No. 3-15974
- *In the Matter of Gordon Brent Pierce*, File No. 3-13109
- *In the Matter of Spring Hill Capital Markets, LLC*, File No. 3-16353
- *In the Matter of Lynn Tilton, et al.*, File No. 3-16462

APPENDIX K

CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES

* * *

C. Related Cases

The case on review has not previously been before this, or any other, Court. Counsel is not aware of any related cases currently pending in this, or any other, Court.

As the Commission previously noted in its letter to the Court dated November 12, 2015 (Doc. No. 1583354), however, and as petitioners note in their brief, a number of other active cases and proceedings involve Appointments Clause challenges to the Commission's use of administrative law judges. In addition to the cases previously listed by the parties, the Commission is aware of the following pending cases that also involve an Appointments Clause challenge to the Commission's use of administrative law judges:[1]

Jacob Keith Cooper v. SEC, No. 15-73193 (9th. Cir.)

Harding Advisory LLC, et al. v. SEC, No. 17-1070 (D.C. Cir.)

Thomas C. Gonnella v. SEC, No. 16-3433 (2d Cir.)

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[1] By listing these cases, the Commission does not acknowledge that the challenges contained therein or in the cases listed by petitioners have been properly presented or preserved.

Malouf v. SEC, No. 16-9546 (10th Cir.)

The Robare Group, LTD., et al. v. SEC, No. 16-1453 (D.C. Cir.)

Bernerd E. Young v. SEC, No. 16-1149 (D.C. Cir.)

Alexander Kon, No. 3-17674 (SEC) & No. 17-3066 (10th Cir.)

* * *

Augustine Capital Management LLC, et al., No. 3-17740 (SEC)

Laurence I. Balter, No. 3-17614 (SEC)

Robert L. Baker, et al., No. 3-17716 (SEC)

Adrian D. Beamish, CPA, No. 3-17651 (SEC)

Bioelectronics Corp. et al., No. 3-17104 (SEC)

Michael W. Crow et al., No. 3-16318 (SEC)

Christopher M. Gibson, No. 3-17184 (SEC)

Donald F. Lathen, Jr., No. 3-17387 (SEC)

RD Legal Capital, LLC & Roni Dersovitz, No. 3-17342 (SEC)

Gary Snisky, No. 3-17645 (SEC)

Paul Leon White II, No. 3-17210 (SEC)

No. 17-130

IN THE
Supreme Court of the United States

RAYMOND J. LUCIA
AND RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

REPLY BRIEF FOR PETITIONERS

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RULE 29.6 STATEMENT

The corporate disclosure statement included in the petition for a writ of certiorari remains accurate.

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REPLY BRIEF FOR PETITIONERS

The question presented is "[w]hether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause." Pet. i. The Solicitor General correctly recognizes that "this Court's resolution of the question presented is necessary." U.S. Br. 26. As the government explains, the answer to that question is "extremely important," and the issue has created "pervasive uncertainty"—including an acknowledged circuit split—in the lower courts. *Id.* at 10. Indeed, the United States now agrees with petitioners that SEC ALJs exercise significant authority under federal law and therefore are Officers who must be appointed pursuant to the Appointments Clause. *Id.* at 14-15. Accordingly, the Court should grant review of the question presented in the petition, and appoint an *amicus curiae* to defend the judgment below. *See id.* at 10.

I. THE COURT SHOULD GRANT CERTIORARI TO DECIDE WHETHER SEC ALJS ARE OFFICERS

The United States agrees that certiorari should be granted in this case, and that the D.C. Circuit's conclusion that SEC ALJs are not Officers was erroneous.

A. The Decision Below Is Wrong

The government now agrees with petitioners that SEC ALJs are Officers within the meaning of the Appointments Clause "because they exercise 'significant authority pursuant to the laws of the United States.'" U.S. Br. 10 (quoting *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam)).

The parties agree that this Court's decision in *Freytag* v. *Commissioner*, 501 U.S. 868 (1991),

"demonstrates" that SEC ALJs are Officers. U.S. Br. 14; *see also* Pet. 14-18. *Every* federal-government official whose position is "established by Law" and who exercises "significant authority pursuant to the laws of the United States is an 'Officer of the United States.'" *Buckley*, 424 U.S. at 126, 132. SEC ALJs undeniably hold offices established by law. Pet. 13-14. And the government now acknowledges that, under *Freytag*, SEC ALJs exercise "significant authority" because they "are authorized, among other things, to administer oaths, hold hearings, take testimony and admit evidence, issue or quash subpoenas, rule on motions, impose sanctions on contemptuous hearing participants, reject deficient filings, and enter default judgments." U.S. Br. 14-15. "Like the special trial judges at issue [in *Freytag*]," SEC ALJs thus undisputedly have "significant 'duties and discretion.'" *Id.* at 14 (quoting *Freytag*, 501 U.S. at 881). In fact, this Court has consistently held that government officials who preside over adjudicatory proceedings in the role of a trial judge exercise significant authority, and are therefore Officers. Pet. 12-13.

The parties further agree that *Freytag* specifically rejected the lynchpin of the decision below—*i.e.*, that an adjudicator is a mere "employee" if he "lack[ed] authority to enter a final decision." 501 U.S. at 880-81; *see* Pet. 20-22; U.S. Br. 16-17. That position "*ignores* the significance of the duties and discretion that special trial judges possess." U.S. Br. 13 (emphasis added) (quoting *Freytag*, 501 U.S. at 881). Indeed, this Court has held that military judges with "no power to render a final decision ... unless permitted to do so by other Executive officers" are Officers. *Edmond* v. *United States*, 520 U.S. 651, 665 (1997). Besides, SEC ALJs can and *do* enter final decisions be-

cause they can enter default judgments, as well as initial decisions that "shall ... be deemed the action of the Commission" if further review is not sought, or a request for such review is denied, 15 U.S.C. § 78d-1(c). *See* Pet. 17; U.S. Br. 15.

As the government correctly explains (at 17-18), *Freytag* cannot be distinguished based on the Tax Court's standard of review or its status as an Article I tribunal. Whatever level of deference the Commission affords an ALJ's findings and decisions, the standard of review in *Freytag* "[wa]s not relevant to [the Court's] grant of certiorari," 501 U.S. at 874 n.3, and "played no role in the Court's conclusion that [special trial judges] qualified as 'Officers.'" U.S. Br. 18. And because "*Freytag* did not even mention [the special trial judges'] status as judicial officials," there is no basis for limiting its holding to Article I courts. *Ibid.*

B. This Case Presents The Best Vehicle To Resolve The Circuit Split

1. The United States agrees with petitioners that "[t]he courts of appeals are divided over whether the Commission's ALJs are officers." U.S. Br. 10. The D.C. Circuit held below that, under its previous interpretation of *Freytag*, SEC ALJs are not Officers because their decisions are subject to discretionary Commission review. Pet. App. 11a-18a (discussing *Landry* v. *FDIC*, 204 F.3d 1125, 1133–34 (D.C. Cir. 2000)). In *Bandimere* v. *SEC*, 844 F.3d 1168 (10th Cir. 2016), the Tenth Circuit squarely rejected that rationale and holding. Expressly "disagree[ing]" with the D.C. Circuit's reading of *Freytag*, the Tenth Circuit concluded that *Freytag* "did not make final decision-making power the essence of inferior officer status." *Id.* at 1182, 1184. SEC ALJs are Officers, the court held, because they "carry out 'important functions,'" *id.* at

1188 (quoting *Freytag*, 501 U.S. at 882), and "'exercis[e] significant authority pursuant to the laws of the United States,'" *ibid.* (quoting *Buckley*, 424 U.S. at 126).

While this petition has been pending, the circuit split has only deepened. *See* U.S. Br. 25. In a case involving ALJs of the Federal Deposit Insurance Corporation, the Fifth Circuit has now joined the Tenth Circuit in disagreeing with the D.C. Circuit's interpretation of *Freytag*: "[C]ontrary to the D.C. Circuit's decision," the Fifth Circuit held, "final decision-making authority is not a necessary condition for Officer status." *Burgess* v. *FDIC*, 871 F.3d 297, 301 (5th Cir. 2017); *see id.* at 301-03 (holding that petitioner had made a "strong showing" that FDIC ALJs are Officers despite their "lack of final decision-making authority").

As the government explains (at 22), this division "has generated substantial confusion and disruption" throughout the administrative state. *See also, e.g.*, Chamber Br. 11-12; PLF Br. 12-15. The Commission has sought or obtained orders holding in abeyance other appellate challenges to the constitutionality of its ALJs. *See, e.g.*, Order, *J.S. Oliver Capital Mgmt.* v. *SEC*, No. 16-72703 (9th Cir. Oct. 25, 2017) (staying appellate proceedings pending disposition of petitions in this case and in *Bandimere*); Order, *Timbervest, LLC* v. *SEC*, No. 15-1416 (D.C. Cir. Aug. 8, 2017) (holding case in abeyance pending disposition of petition in this case); SEC Rule 28(j) Letter, *Bennett* v. *SEC*, No. 16-3827 (8th Cir. Nov. 29, 2017) (requesting abeyance pending disposition of petition in this case). Accordingly, "the Commission's ability to enforce the nation's securities laws has, in significant respects,

been put on hold" until the Court decides *this* case. U.S. Br. 25.

2. The government also agrees with petitioners that "this case, rather than *Bandimere*, presents the Court with the preferable vehicle" for resolving the circuit split. U.S. Br. 24; *see also* Pet. 35 n.*. Unlike *Bandimere*—from which Justice Gorsuch may be recused—this case presents a clean opportunity for the full Court to decide whether SEC ALJs are Officers. *See* Br. for *Amici Curiae* Raymond J. Lucia and Raymond J. Lucia Cos. at 5-7, *SEC* v. *Bandimere*, No. 17-475 (U.S. Oct. 24, 2017). The question presented has been fully ventilated in the extensive proceedings below—including rehearing before the en banc D.C. Circuit—and there are no jurisdictional, preservation, or other problems that could prevent the Court from deciding the Officer question.

C. Recent Developments Do Not Moot This Case

Two significant developments have occurred since the filing of the petition: The government now agrees that SEC ALJs are Officers; and one day after the government filed its brief confessing error, the Commission issued an order purporting to "ratifly] the agency's prior appointment" of its current ALJs. Order, *In re Pending Administrative Proceedings*, Securities Act Release No. 10,440, at 1 (Nov. 30, 2017) ("Ratification Order"). Neither development moots this case nor diminishes the need for this Court's review.

1. Although the government now agrees that SEC ALJs are Officers, it has afforded petitioners no redress for having subjected them to trial before an unconstitutionally constituted tribunal. *See* U.S. Br. 20-

21. On the contrary, petitioners remain subject to draconian sanctions—including a *lifetime* associational bar—resulting from the tainted proceedings below. *Id.* at 6. The court of appeals sustained those sanctions, which continue to have devastating effects on Ray Lucia. Absent review by this Court, the judgment below will stand uncorrected notwithstanding the Justice Department's confession of error. Review and reversal are warranted to provide petitioners a meaningful remedy for the constitutional deprivation they have suffered.

The government has not yet dismissed the proceedings against petitioners, and therefore there remains a case or controversy between them. In light of the government's change in position regarding whether SEC ALJs are Officers, however, the Court may wish to appoint an *amicus curiae* to defend the judgment below.

2. By its own terms, the Commission's so-called Ratification Order has no applicability to this case; it is also substantively defective.

a. The so-called Ratification Order does not render this case moot. *See Knox* v. *Serv. Emps. Int'l Union*, 567 U.S. 298, 307 (2012) ("voluntary cessation of challenged conduct does not ordinarily render a case moot"). Absent this Court's review, nothing would prevent the Commission from *continuing* to assert that its ALJs are employees. As the Order itself makes clear, unless and until this Court decides the question presented, the Commission will not actually acknowledge that petitioners were tried by an unconstitutional adjudicator or provide an appropriate remedy for that constitutional violation.

The so-called Ratification Order has no effect on this case because by its own terms it applies only to enforcement actions still pending in the administrative process, not to cases that are now pending before an Article III court. *See* Ratification Order 1-2; *see also id.*, Ex. A (listing proceedings remanded to ALJs). Having completed the administrative process, petitioners are entitled to a meaningful remedy for the constitutional deprivation they have suffered. In fact—as petitioners have repeatedly noted without any objection from the Commission or the Department of Justice—the Commission has waived or forfeited any argument in *this* case that "the Appointments Clause violation could be excused under a harmless-error, ratification, *de facto* officer, or any other similar doctrine." Pet. 34; *see also* Pet. App. 9a-10a. No thirteenth-hour ratification can salvage petitioners' tainted adjudication or the ensuing decisions and order.

As the United States appears to concede (at 20-21), petitioners at minimum are "entitled to a hearing before a properly appointed [ALJ]." *Ryder* v. *United States*, 515 U.S. 177, 188 (1995); *see also United States* v. *L.A. Tucker Truck Lines, Inc.*, 344 U.S. 33, 38 (1952). For example, this Court has vacated the judgment of a panel with a *single* ineligible member, even though the remaining panel members provided "a quorum of judges competent to consider the appeal." *Nguyen* v. *United States*, 539 U.S. 69, 82 (2003). And the Court has held that a litigant tried before one biased judge must receive an entirely new trial before an impartial adjudicator. *Tumey* v. *Ohio*, 273 U.S. 510, 535 (1927). It is therefore clear that the Commission cannot simply wave a wand and reinstate any of the findings or conclusions made by the ALJ in this case. Because the Appointments Clause violation is a

"structural" error, *Freytag*, 501 U.S. at 878-79, the Commission's *only* options will be to dismiss the proceedings or seek a new proceeding before a constitutional tribunal—either a properly appointed ALJ other than Cameron Elliot, or a federal district judge.

b. The so-called Ratification Order has no effect on any other case, either, because SEC ALJs still have not been *appointed* in conformity with the Appointments Clause.

The Order (at 1) instead purports to "ratif[y] the agency's prior appointment" of five identified ALJs. But there undisputedly was no prior agency "appointment" to ratify because, as the government acknowledges (U.S. Br. 19), the Commission "did not play any role in the selection" of those ALJs. Rather, as "employ[ee]s" of the Commission, SEC ALJs had been "hired"—not appointed—by the SEC's Chief ALJ from a list prepared by the Office of Personnel Management, with few exceptions. U.S. Br. 3; *see also, e.g.*, Pet. App. 296a-297a (ALJ Elliot selected through this "hiring process"). The Commission conceded below that this method did not comport with the Appointments Clause. Pet. App. 9a. The "ratification" of an unconstitutional procedure is itself a nullity.

This result follows directly from the "principles of agency law" that "presumptively" govern ratification. *FEC* v. *NRA Political Victory Fund*, 513 U.S. 88, 98 (1994). Ratification operates only to grant retroactive effect to an unauthorized act "as though authority to do the act *had been previously given*." *Cook* v. *Tullis*, 85 U.S. 332, 338 (1874) (emphasis added). Because the Appointments Clause barred the Commission from giving the Chief ALJ authority to "hire" other ALJs (*i.e.*, Officers) in the first place, the Commission has no power to ratify that "hiring" retroactively.

NRA Political Victory Fund, 513 U.S. at 98 ("it is essential that the party ratifying should be able ... to do the act ratified ... *at the time the ratification was made*" (quoting *Cook*, 85 U.S. at 338)). SEC ALJs must be *appointed* by the Commission itself—and this Order does not do that. Indeed, petitioners are aware of no "evidence of an appointment," such as the signature and delivery of a commission to the Commission's ALJs. *Marbury* v. *Madison*, 5 U.S. (1 Cranch) 137, 157 (1803); *see* U.S. Const. art. II, § 3 (requiring "all the officers of the United States" to receive a commission).

II. The Removal Issue Is Not Properly Presented

After agreeing that the Court should grant review in this case to decide whether SEC ALJs are Officers, the Solicitor General asks this Court to *also* decide whether limitations on the removal of SEC ALJs from office violate the separation of powers. U.S. Br. 18-21. Yet the government does not dispute petitioners' previous explanation that "the constitutionality of ALJ removal procedures ... ha[s] never been raised by any party in this case (or in *Bandimere*) and thus th[is is] not [an] argument[] available to the government here." Pet. 34.

It is canonical that this Court is "a court of review, not of first view." *Cutter* v. *Wilkinson*, 544 U.S. 709, 718 n.7 (2005). Although petitioners have "reserve[d] the right to raise" the removal issue in the unlikely event that this case involves further proceedings before a properly appointed ALJ, Opening Br. for Petitioners at 54 n.6, *Raymond J. Lucia Cos.* v. *SEC*, 868 F.3d 1021 (D.C. Cir. 2017) (en banc) (No. 15-1345), that issue was neither pressed nor passed on in any of the proceedings below—the government even refused

to take a position on the issue despite multiple questions at oral argument. *Hear* Oral Argument at 59:19-1:02:01, *Raymond J. Lucia Cos.* v. *SEC*, 868 F.3d 1021 (D.C. Cir. 2017) (en banc) (No. 15-1345), https://tinyurl.com/yddcpeyh (last visited December 12, 2017). Nor is the removal issue even remotely encompassed by petitioners' question presented. *See Yee* v. *City of Escondido*, 503 U.S. 519, 535 (1992) ("While we have on occasion rephrased the question presented by a petitioner, ... by and large it is the petitioner himself who controls the scope of the question presented" (citations omitted)).

In fact, no court of appeals has decided whether SEC ALJs' removal protections are unconstitutional. *See, e.g.*, *Bandimere*, 844 F.3d at 1188 ("Questions about officer removal ... are not issues on appeal and have not been briefed by the parties"). The Solicitor General thus asks this Court to break new ground without the benefit of a decision from the court below or any other court of appeals.

In *Free Enterprise Fund* v. *Public Company Accounting Oversight Board*, 561 U.S. 477 (2010), the Court held that "dual for-cause limitations on the removal" of members of the Public Company Accounting Oversight Board (PCAOB) violate the Constitution's separation of powers. *Id.* at 492. But the Court expressly "d[id] not address" similar removal protections for ALJs because it was "disputed" whether ALJs are necessarily Officers, and "[t]he Government below refused to identify ... administrative law judges as 'precedent for the PCAOB.'" *Id.* at 507 n.10 (citation omitted).

Similar prudence would be especially appropriate here. If the Court holds that SEC ALJs are Officers, the Commission's decision and order must be vacated.

If the proceeding is dismissed, or petitioners are afforded a new trial in an Article III forum, the removal issue would never be presented in this case. The government thus seems to ask the Court to provide an advisory opinion on the removal issue. Only if the Commission attempts to try petitioners again before a properly appointed ALJ (assuming, *dubitante*, that such a trial could conform to minimum due process requirements) would the removal issue arise in this case. In that unlikely event, petitioners would raise the removal issue as a constitutional objection or defense to adjudication before an SEC ALJ. Resolving that issue would require, among other things, determining whether the SEC Commissioners *themselves* enjoy for-cause removal protection. *See* U.S. Br. 20.

If the Court nevertheless is inclined to decide the removal issue now, petitioners respectfully request that the Court formulate a specific question on that issue. The Court has previously framed its own questions on constitutional issues. *See, e.g.*, *NLRB* v. *Noel Canning*, 133 S. Ct. 2861 (2013). The Solicitor General proposes the unitary question whether the Commission's "use of administrative law judges as hearing officers ... violates constitutional limitations on 'Officers of the United States.'" U.S. Br. i. But that reframing is unnecessarily broad. Petitioners propose instead the following additional question: "Whether limitations on the removal of SEC ALJs violate the separation of powers."

CONCLUSION

The petition for a writ of certiorari should be granted limited to the question presented in the petition.

Respectfully submitted.

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RECORD AND BRIEFS

No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, ET AL.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF FOR CATO INSTITUTE AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Can an executive agency's officers investigate, prosecute, and adjudicate disputes without oversight from the chief executive?

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INTEREST OF THE *AMICUS CURIAE*[1]

The Cato Institute was established in 1977 as a nonpartisan public policy research foundation dedicated to advancing the principles of individual liberty, free markets, and limited government. Cato's Center for Constitutional Studies was established in 1989 to promote the principles of limited constitutional government that are the foundation of liberty. Cato's Center for Monetary and Financial Alternatives was established in 2014 to reveal the shortcomings of today's monetary and financial regulatory systems and to identify and promote alternatives more conducive to a stable, flourishing, and free society. Toward those ends, Cato publishes books and studies, conducts conferences, issues the annual *Cato Supreme Court Review*, and files *amicus* briefs with the courts.

This case is important to Cato because it regards core separation-of-powers issues and the democratic accountability of executive officers.

INTRODUCTION AND SUMMARY OF ARGUMENT

The Constitution created three branches of government. The legislative and executive branches are controlled by the electorate. The president is vested with all executive power, and therefore controls the executive branch. 1 Annals of Cong. 481 (James Madison, June 16, 1789) ("[I]f any power whatsoever is in its na-

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[1] Rule 37 statement: All parties were timely notified of *amicus*'s intent to file this brief; Petitioners lodged a blanket consent with the Clerk, while Respondent consented by particular letter. No party's counsel authored any part of this brief and no person other than amicus funded its preparation and submission.

ture executive, it is the power of appointing, overseeing, and *controlling* those who execute the laws.") (emphasis added). The president has a duty to see that the law is faithfully executed. To do this he must be able to remove those officers who fail in their duties.

And yet, the SEC's administrative law judges (ALJs) are protected from control by the electorate. The president lacks the ability to remove ALJs should they abuse their powers or fail to use their discretion to act intelligently or wisely.

The D.C. Circuit ruled that ALJs need not be subject to presidential removal power because they are not executive officers. When the same case was reheard *en banc*, the court deadlocked, five to five, leaving in place the panel's earlier characterization of ALJs as something less than the category of officers constitutionally subject to presidential removal.

But ALJs' duties are similar to Special Trial Judges (STJs) and court clerks, positions the Court has previously determined to be officers. If anything, ALJs have more power and exercise their duties with greater discretion and independence than STJs or court clerks.

The similarities between ALJs and court clerks and STJs should be sufficient evidence to show that ALJs are officers. Still, it is worth further noting that ALJs also fit definitions of an "executive officer" established by important legal and historical precedents. Chief Justice John Marshall delineated a test for distinguishing an officer from an employee. Writing for the Court in *United States v. Maurice*, 26 F. Cas. 1211 (C.C.D. Va. 1823), he explained that if a position did not require a contract for its holders because the gov-

ernment had prescribed the position's duties independent of a specific position-holder and that the duties of successive position-holders would not change, then that position should be classified as an office. The Court later expanded on Marshall's initial criterion by setting parameters for the tenure, duration, emolument, and duties of an officer, parameters that distinguish an officer from an employee. Evaluating the ALJ position against these parameters demonstrates that ALJs are officers, not employees. Most importantly, ALJs have significant discretion and perform more than ministerial duties, which, based on the Court's definitions, should clearly make ALJs officers.

Both Congress and the SEC have recognized that ALJs are officers. Considering how much more closely the ALJ position aligns with the definition of an officer than the definition of an employee, this should not be a surprise.

The quasi-judicial nature of ALJs' role does not change their status as officers. The Court established that presidential accountability applies to officers with a quasi-judicial function 90 years ago. It held that even for a quasi-judicial executive officer, the president "may consider the decision after its rendition as a reason for removing the officer, on the ground that the discretion regularly entrusted to that officer by statute has not been on the whole intelligently or wisely exercised." *Myers v. United States*, 272 U.S. 52, 135 (1926). Precedent going back to the Founding also support the notion that SEC ALJs must be subject to executive oversight. The Comptroller of the Treasury was then considered quasi-judicial for the same reasons an ALJ could be considered such today, yet could still be re-

moved by the president. The president has also removed territorial judges, demonstrating that the judicial character of an executive-branch officer does not change the president's authority to remove that officer.

This case presents a fundamental challenge to the principles underpinning the appointments clause. Moreover, the issue is ripe for review. Not only has the D.C. Circuit deadlocked on the question, but in a recent case, the 10th Circuit ruled in *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016), that ALJs are indeed officers. There is therefore a clear split between the circuits, which can only be resolved by this Court. The Court should take this case and affirm that ALJs are officers who must be appointed in accordance with Article II of the Constitution.

ARGUMENT

I. SEC ALJS ARE EXECUTIVE OFFICERS BECAUSE OF THEIR DISCRETION AND POWER

ALJs are officers, not employees, because of the discretion they wield and the power they exercise. The close similarities between on the one hand ALJs and on the other STJs and court clerks—positions that the Court has deemed are offices—are sufficient proof that ALJs are officers. In addition, ALJs clearly fit important legal and historical definitions of officers.

A. ALJs Have Duties and Powers Similar to Other Quasi-Judicial Positions That the Court Has Ruled Are Offices

In *Freytag v. C.I.R.*, the Court determined that STJs are executive officers because of the discretion and power they exercise. 501 U.S. 868, 881-82 (1991).

There is no material difference between the discretion and power STJs and SEC ALJs exercise. Like the *Freytag* STJs, SEC ALJs "perform more than ministerial tasks." *Id.* at 881. They too "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders." *Id.* at 881-82; 17 C.F.R. §201.111. And, like STJs, ALJs "exercise significant discretion in the course of carrying out their duties." *Freytag*, 501 U.S. at 881-82; 17 C.F.R. §201.111. ALJs notably use their discretion to make findings as to the credibility of witnesses and the SEC defers to ALJs' "credibility finding, absent overwhelming evidence to the contrary." *In re Clawson*, Exchange Act Release No. 48143, 2003 WL 21539920, at *2 (July 9, 2003); *In re Pelosi*, Securities Act Release No. 3805, 2014 WL 1247415, at *2 (Mar. 27, 2014) ("The Commission gives considerable weight to the credibility determination of a law judge since it is based on hearing the witnesses' testimony and observing their demeanor. Such determinations can be overcome only where the record contains substantial evidence for doing so."); *Universal Camera Corp. v. N.L.R.B.*, 340 U.S. 474, 496 (1951). Moreover, the opinions ALJs issue are final unless appealed and *Freytag* emphasized the importance of STJs' power to issue opinions. 5 U.S.C. § 557(b); *Freytag*, 501 U.S. at 882 (noting that the fact that the STJ can "render the decisions of the Tax Court" in some cases is enough to be considered an officer).

The ALJs' authority also mirrors that of the court clerks, which, under the Court's determination, rendered them officers. *See Ex parte Hennen*, 38 U.S. 230, 260 (1839) ("These clerks fall under that class of inferior officers, the appointment of which the Constitution authorizes Congress to vest in the head of the

department."). This despite the fact that clerks have no power to make final decisions for the court outside of default judgments (which can be rescinded by the court). FRCP 77(2); FRCP 55(b)(1). As do ALJs, 17 C.F.R. § 201.155, and reject deficient filings as some clerks can, 17 C.F.R. § 201.180 (b), (c). Clerks can administer oaths and affirmations, 28 U.S.C. § 953, as can ALJs. 17 CFR 201.111(a). There is no power or discretion that such clerks have that an ALJ does not. Since a clerk is an "officer of the United States" due to these powers, an ALJ must also be an officer.

The panel ruled that SEC ALJs are not officers because their decisions are not final (in that they are appealable to the Commission). *Raymond J. Lucia Cos., Inc. v. SEC*, 832 F. 3d 277, 285 (D.C. Cir. 2016). This argument must not be taken too far since no one would suggest that district court judges, whose opinions are appealable to the circuit court, are not officers. But even given limited application, it fails in the face of respondents' actual experience appearing before SEC ALJs. Although ALJs' rulings on questions of law are subject to review, their findings of fact are nearly unassailable and are given great deference by the Commission. This is, of course, assuming that a respondent proceeds so far as to obtain an appealable decision. As many as half of SEC enforcement actions result in settlement with up to 80 percent of those settlements brought in administrative proceedings. Urska Velikonja, *Securities Settlements in the Shadows*, 126 Yale L.J. Forum 124 (2016). The tenor of administrative proceedings, set in the SEC almost exclusively by the ALJs, inform both respondents' decisions and their counsels' admonitions regarding the wisdom of settlement. If most respondents never make their case before the Commission and if those who do are almost

unfailingly bound by the factual determinations of the ALJs, it is difficult to see how the existence of such limited review can be controlling. If it is true that "[w]ise observers have long understood that the appearance of justice is as important as its reality," it must also be true that appearance of justice does not trump actual injustice in practice. *J.E.B. v. Ala. ex rel. T.B.*, 511 U.S. 127, 161 n.3 (1994) (Scalia, J., joined by Rehnquist, C. J., and Thomas, J., dissenting).

There are also important historical precedents for considering SEC ALJs to be officers. At the Founding, jurists understood that a position must be an office and its holder an officer if executing the duties of that position entailed exercising coercive authority over others. "It is a rule, that where one man hath to do with another's affairs against his will, without his leave, that is an office, and he who is in it, an officer." Giles Jacob, A New Law Dictionary 641 (10th ed. 1773). It is unlikely that respondents hand the SEC penalties of their own free will, and therefore ALJs exercise the type of authority that Jacob described. 17 C.F.R. § 201.155.

B. SEC ALJs Fit Legal Precedents and Definitions of Officers

The first Supreme Court justice to consider the characteristics that distinguish officers from employees was Chief Justice John Marshall in *United States v. Maurice*, 26 F. Cas. 1211 (C.C.D. Va. 1823). That case required the Court to determine if an agent for fortifications was an officer of the United States. The opinion in that case established general criteria for determining whether a position is or is not an office:

> An office is defined to be "a public charge or employment," and he who performs the duties of the office, is an officer. If employed on the part of the United States, he is an officer of the United States. Although an office is "an employment," it does not follow that every employment is an office. A man may certainly be employed under a contract, express or implied, to do an act, or perform a service, without becoming an officer. But if a duty be a continuing one, which is defined by rules prescribed by the government, and not by contract, which an individual is appointed by government to perform, who enters on the duties appertaining to his station, without any contract defining them, if those duties continue, though the person be changed; it seems very difficult to distinguish such a charge or employment from an office, or the person who performs the duties from an officer.

Id. at 1214. To Marshall, it was the lack of a contract to perform a service in which different people may consecutively hold the same position that distinguishes an "office" from employment. *Maurice*, 26 F. Cas. at 1214. The Court cited Marshall's definition of an office in a later case regarding the status of a merchant appraiser. *Auffmordt v. Hedden*, 137 U.S. 310, 327 (1890). Marshall's definition applies to an SEC ALJ, who is not under contract to perform a service but "enters on the duties appertaining to his [or her] station" and that "those duties continue, though the person be changed." The criteria that Marshall delineated and that the Court applied in *Auffmordt* provide further support for classifying SEC ALJs as officers. *See Id.* 5 U.S.C. § 3105.

The Court issued another, more comprehensive definition of an office in *United States v. Hartwell*, 73 U.S. 385 (1867), a definition ALJs fit. The Court held that "an office is a public station, or employment, conferred by the appointment of government" and that "[t]he term embraces the ideas of tenure, duration, emolument, and duties." *Id.* at 393. The Court applied each of these requirements to its definition of an officer. An officer is someone "appointed pursuant to law, and his compensation was fixed by law." *Id.* An ALJ is likewise appointed pursuant to law and the compensation is fixed by law. 5 U.S.C. § 3105; 5 U.S.C. § 5372. The Court then noted that "[v]acating the office of his superior would not have affected the tenure of his place," *Hartwell*, 73 U.S. at 393, which shows the independent nature of an office. An ALJ's tenure is likewise unaffected by the removal of any other person from office. The Court finally recognized the "duties were continuing and permanent, not occasional or temporary," *id.*, which accurately describes an ALJ's duties, 5 U.S.C. § 7521.

In more recent cases, the Court expanded on that definition to require that a position holder must be "exercising significant authority" to be considered an officer. *Buckley v. Valeo*, 424 U.S. 1, 126 (1976). This expansion was not meant to challenge prior understandings of an officer's status, but rather affirmed and crystalized the reasoning that led the Court to determine that district court clerks and postmasters first class are inferior officers. *Id. Buckley's* definition of an officer included "all appointed officials exercising responsibility under the public laws of the Nation." *Id.* at 131. ALJs easily fit this definition.

In *Buckley*, the Court distinguished employees from officers by describing them as "lesser functionaries subordinate to officers of the United States." *Id.* The Court's decision in *Freytag* reflected this distinction, as it determined that special trial judges are officers because they "perform more than ministerial tasks" and exercise "significant discretion." *Freytag*, 501 U.S. at 881-82. *Buckley's* emphasis on the relative independence of a position and its organizational relationship to other officers closely pertains to SEC ALJs also. The statutory framework governing the authority of ALJs ensures that they are not directly controlled by any other officer. 5 U.S.C. § 7521(a).

Considering the independence of and discretion wielded by the SEC's ALJs in the context of relevant historical and legal precedents, it is no wonder that Congress considers ALJs to be officers. The SEC's enabling statute states that ALJs' authority to hold hearings is predicated upon their status as officers. 15 U.S.C. § 77u ("All hearings shall be public and may be held before the Commission or an *officer or officers* of the Commission designated by it.") (emphasis added); *see also* 17 C.F.R. § 201.111 (SEC regulation referring to an ALJ as a "hearing officer").

II. ADMINISTRATIVE LAW JUDGES' PROTECTION FROM REMOVAL IS UNCONSTITUTIONAL UNDER THE APPOINTMENTS CLAUSE

The Constitution guarantees that even officers who are appointed (not elected) are nonetheless accountable to the people. Although the Constitution offers no explicit guidance on removals, jurists have understood that removals "empower the President to keep these

officers accountable" including through the removal of the officers if necessary. *Free Enter. Fund v. Pub. Co. Acc'ting Oversight Bd.*, 561 U.S. 477, 483 (2010).

A. ALJs Must Be Removable by the President to Ensure Democratic Accountability for Executive Officers

Since the Founding, jurists have understood that the president, to fulfill his constitutional duty to ensure that the laws be faithfully executed, must have the power to remove executive officers. The Constitution does not specify how an officer can be removed (other than impeachment), and so a debate occurred in the First Congress over the presidential power to remove officers. Some felt that impeachment was the only proper method of removal because it was the only one specifically mentioned. James Madison disagreed, declaring that "it is absolutely necessary that the President should have the power of removing from office; it will make him, in a peculiar manner, responsible for their conduct, and subject him to impeachment himself, if he suffers them to perpetrate with impunity high crimes or misdemeanors against the United States, or neglects to superintend their conduct, so as to check their excesses." 1 Annals of Congress 387 (1789). Such a power to remove officers was seen at the time as "incident to the power of appointment." *Myers*, 272 U.S. at 110 (1926).

Madison did not consider this power to remove to be absolute, but "because Congress may establish offices by law," Congress could decide if the officer's tenure was "either during good behavior or during pleasure." 1 Annals of Congress 389 (1789). In the end of the

debate, the First Congress by a "considerable majority" resolved "the power of removal to be in the President." *Id.* at 399.

Despite Congress's authority to grant tenure for good behavior, as of 1903 "no civil officer [had] ever held office by a life tenure since the foundation of the government" with the exception of Article III judges. *Shurtleff v. United States*, 189 U.S. 311, 316 (1903). When Congress attempted to condition the removal of a postmaster on congressional approval, the Court held that to be an unconstitutional limitation on the power of the president. *Myers*, 272 U.S. at 176.

If a limitation on the president's removal power is unconstitutional, it is immaterial which entity exercises the limitation. If it is unconstitutional to condition the president's removal power on the Senate's consent, it is equally unconstitutional to condition the removal power on the consent of the Merit Systems Protection Board (MSPB). As Madison said, if the executive officer "shall not be displaced but by and with the advice and consent of the senate, the President is no longer answerable for the conduct of the officer; all will depend on the senate. You here destroy a real responsibility without obtaining even the shadow." 1 Annals of Congress 394-95. Likewise, the president is not fully answerable for the conduct of ALJs if they cannot be removed without the advice and consent of the MSPB (which also cannot be removed but for cause). When an ALJ goes beyond the powers of that office, but the MSPB refuses exercise its removal power, which elected official are the American people to blame?

B. SEC ALJs Are Not Democratically Accountable, Because Their Removal Involves Two Layers of Protection

SEC ALJs are inferior officers that are protected from presidential removal by at least two layers of for-cause removal protection. Permitting an executive officer to enjoy such insulation from removal unconstitutionally prevents the president from exercising the necessary control to be politically accountable for the actions of the officer. *Free Enter. Fund*, 561 U.S. at 477.

The first layer of protection exists at the SEC level. The SEC can only remove an ALJ "for cause." 5 U.S.C. § 7521(a). Second, that determination of cause must be confirmed by the MSPB. MSPB members themselves can only be removed "for cause." *Id.*; 5 U.S.C. § 1202. Therefore, the judgment that an SEC ALJ should be removed for cause is "committed to another officer, who may or may not agree with the president's determination, and whom the President cannot remove simply because that officer disagrees with him." *Free Enter. Fund*, 561 U.S. at 484. Moreover, *Free Enterprise Fund* established that SEC commissioners themselves are only removable for cause, *Id.* At 487. Assuming that the Court was correct in *Free Enterprise Fund*, there exist in fact three layers of protection between SEC ALJs and the president. SEC commissioners themselves must initiate the removal proceedings against ALJs. 5 U.S.C. § 7521(a).

C. Even Officers in Quasi-Judicial Roles Like ALJs Must Be Removable by the President

Historical precedent going back to the Founding and this Court's direct on-point holdings show that even federal officials serving "quasi-judicial" roles like the ALJ position must be removable by the president.

The Court has held that even executive officers with a quasi-judicial role (such as ALJs) must not be beyond the president's power to remove any officer who fails to exercise the discretion required of the office intelligently or wisely. As it said in *Myers*:

> Then there may be duties of a quasi judicial character imposed on executive officers and members of executive tribunals whose decisions after hearing affect interests of individuals, the discharge of which the President cannot in a particular case properly influence or control. But even in such a case he may consider the decision after its rendition as a reason for removing the officer, on the ground that the discretion regularly entrusted to that officer by statute has not been on the whole intelligently or wisely exercised. Otherwise he does not discharge his own constitutional duty of seeing that the laws be faithfully executed. 272 U.S. at 135.

The president's power to remove quasi-judicial officers is not absolute like the power to remove purely executive officers; Congress can limit the removal of such quasi-judicial officers to "for-cause" reasons. *Humphrey's Executor v. United States*, 295 U.S. 602, 629 (1935). The removal for-cause still allows the

president to see that the laws "be faithfully executed" but only so long as the president exercises direct authority to remove the officer for cause, or the power is exercised by an individual the president can remove without cause. *Free Enter. Fund*, 561 U.S. at 495-96.

Historical precedent also shows that quasi-judicial executive officers must be subject to presidential removal power. The first discussion of a quasi-judicial executive officer's removal occurred during the First Congress when considering the removal of the Comptroller of the Treasury. The Comptroller of the Treasury, due to his authority to decide claims between the United States and individual citizens, exercised power that was "not purely executive" but also included a "judicial quality." 1 Annals of Congress 635-36 (1789). Because of the quasi-judicial character of the office, Madison proposed that the tenure of the office be for "good behavior," but even so "the Comptroller would be dependent upon the President, because he can be removed by him." *Id.* Tenure based only on "good behavior" was necessary to "secure his impartiality," but even the need for impartiality was not sufficient to shield the officer entirely from the president's removal power. *Id.* This for cause protection was too much for many of the other members of the First Congress and Madison eventually withdrew his motion. *Id.* at 637-39. The Court revived Madison's position in *Humphrey's Executor*, implementing his idea of limiting the removal of quasi-judicial executive officers. Still, the president retained the power to remove the quasi-judicial officer for cause.

ALJs fulfill a more purely judicial function than either members of the Federal Trade Commission or

the Comptroller of the Treasury. Their role may be more properly analogous to other non-Article III federal judges. While the president has never removed an Article III judge—the Constitution insulates them from such action—the president has removed many Article I judges (such as territorial judges) without even giving cause and without congressional authorization. The power to remove these judges has been viewed as essential to the president's ability to fulfill his duty. Before the Civil War, Attorney General John J. Crittenden was specifically asked about the presidential power to remove territorial judges, even without congressional authorization. He concluded:

> The President of the United States is not only invested with authority to remove the Chief Justice of the Territory of Minnesota from office, but it is his duty to do so if it appear that he is incompetent and unfit for the place. . . . Being civil officers, appointed by the President, by and with the advice and consent of the Senate, and commissioned by the President, they are not exempted from that executive power which, by the constitution, is vested in the President of the United States over all civil officers appointed by him.

5 U.S. Op. Atty. Gen. 288, 290 (1851). He opined that this removal power "has been long since settled, and . . . has ceased to be a subject of controversy or doubt." *Id.*

In *McAllister v. United States* the Court interpreted the general statutory provisions for removal and replacement of "any civil officer . . . except judges of the courts of the United States" by the president as allowing the president to remove territorial judges.

141 U.S. 174 (1891). The quasi-judicial character of the office did not change the power of the president to remove such executive officers.

When considering Congress's removal of the Comptroller General, the Court stated that "[i]nterpreting a law enacted by Congress to implement the legislative mandate" and "exercis[ing] judgment concerning facts that affect the application of the Act" are "[d]ecisions of that kind are typically made by officers charged with executing a statute." *Bowsher v. Synar*, 478 U.S. 714, 733 (1986).

The D.C. Circuit, in *Kuretski v. C.I.R*, also considered the presidential removal of tax judges. In that case, the court held: "A tribunal may be considered a 'Court of Law' for purposes of the Appointments Clause notwithstanding that its officers may be removed by the President. The *Freytag* Court's treatment of territorial courts confirms the point." *Kuretski v. C.I.R.*, 755 F.3d 929, 941 (D.C. Cir. 2014), *cert. denied*, 135 S. Ct. 2309 (2015).

These examples include executive officers' exercising quasi-judicial functions as well as Article I judges that preside over a "court of law." ALJs sit somewhere in the middle of this continuum. That it is well-settled that the president must have the power to remove officers sitting at both ends of this spectrum confirms that he must have the power to remove for cause officers sitting in the middle of it.

CONCLUSION

Our Constitution requires that our government remain democratically accountable, so *amicus* asks the Court to take this case and to determine that ALJs are officers of the United States and therefore removable by the president.

Respectfully submitted,

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RECORD AND BRIEFS

No. 17-130

In the Supreme Court of the United States

RAYMOND J. LUCIA
AND RAYMOND J. LUCIA COMPANIES, INC.,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICUS CURIAE* SUPPORTING PETITIONERS

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BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

INTEREST OF THE *AMICUS CURIAE*

The Chamber of Commerce of the United States of America is the world's largest business federation. It represents 300,000 direct members and indirectly represents the interests of more than 3 million companies and professional organizations of every size, in every industry sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus curiae* briefs in cases that raise issues of concern to the nation's business community.[1]

Businesses are frequently respondents in enforcement actions by the Securities and Exchange Commission ("SEC"). The Chamber accordingly has an interest in ensuring that the power to preside over those proceedings and to affect the interests of those businesses is vested in officials who are constitutionally appointed.

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[1] Pursuant to Rule 37.6, *amicus* affirms that no counsel for a party authored this brief in whole or in part and that no person other than *amicus*, its members, or its counsel made a monetary contribution to its preparation or submission. Counsel of record for all parties received notice at least 10 days prior to the due date of the intention of *amicus* to file this brief. The parties' letters consenting to the filing of this brief have been filed with the Clerk's office.

SUMMARY OF ARGUMENT

The question presented in this case plainly warrants review by this Court. The issue is important; there is a square conflict among the lower courts; and the lower courts' conflicting holdings turn on differing interpretations of this Court's precedents—an issue that only this Court can resolve.

The Securities and Exchange Commission brought 692 administrative enforcement actions in fiscal year 2016—80% of all of the enforcement actions instituted.[2] Every one of those administrative proceedings was presided over by an administrative law judge ("ALJ") who was not appointed by the President or by the Commission. Every one of those proceedings therefore implicates the important question presented here regarding the application of the Appointments Clause.

The Appointments Clause protects against the manipulation and abuse of "the most insidious and powerful weapon of eighteenth century despotism"—"the power of appointment to offices." *Freytag* v. *Comm'r*, 501 U.S. 868, 883 (1991). The Framers sought to prevent abuse of the appointment power by limiting the dispersion of that authority and ensuring that "those who wielded it were accountable to political force and the will of the people." *Id.* at 884. Thus, all officers—*i.e.*, any official "exercising significant authority pursuant to the laws of the United States," *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976)—

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[2] Securities & Exchange Comm'n, Select SEC and Market Data Fiscal 2016 at 3 tbl. 2, https://www.sec.gov/files/2017-03/secstats2016.pdf.

must be appointed by the President "with the Advice and Consent of the Senate," or, in the case of inferior officers, by "the President alone, in the Courts of Law, or in the Heads of Departments," as directed by Congress. U.S. CONST. art. II, § 2, cl. 2.

This Court's precedents compel the conclusion that SEC ALJs are "officers" subject to the Appointments Clause. SEC ALJs exercise significant authority over the business community: They may preside over administrative proceedings brought by the SEC against *any* business or individual; in the course of those proceedings, they receive and rule on the admissibility of evidence, issue subpoenas, rule on dispositive and procedural motions, and regulate the course of the hearing; and at the conclusion of the proceedings, they may issue initial decisions that declare respondents liable and impose sanctions ranging from monetary penalties to barring individuals from associating with others in the securities industry. In 90% of proceedings, their initial decisions become final without any review or revision from an SEC Commissioner.

The three-judge panel of the D.C. Circuit instead eviscerated the structural safeguards of the Appointments Clause, holding that SEC ALJs are not officers who must be appointed in accordance with the Appointments Clause based solely on the fact that they do not possess the authority to enter final decisions; after an en banc rehearing, the D.C. Circuit split evenly, leaving in place the panel opinion. See D.C. Cir. R. 35(d).

The D.C. Circuit's misapplication of this Court's precedents places it directly at odds with the Tenth Circuit, which correctly held that SEC ALJs are "officers" subject to the Appointments Clause. See

Bandimere v. *S.E.C.*, 844 F.3d 1168, 1188 (10th Cir. 2016).

After *Bandimere*, the Commission stayed all administrative proceedings in which the respondent has the option of seeking review in the Tenth Circuit of the final order of the Commission, leaving the fate of those businesses and individuals in limbo; at the same time, the Commission continues to proceed administratively in large numbers against those businesses and individuals who happen to be located outside of the geographical bounds of the Tenth Circuit. *Amicus* respectfully submits that this Court's review of the decision below is warranted to ensure uniform—and proper—application of the Appointments Clause.

ARGUMENT

I. The Constitutional Standards Governing Appointment Of SEC ALJs Is An Issue Of National Importance.

Over the past decade, the number of enforcement proceedings presided over by SEC ALJs has dramatically increased—both in absolute terms and relative to the number of enforcement actions brought by the Commission as civil actions in court. That transformation results largely from statutory changes expanding the categories of persons who may be targeted through administrative actions and the remedies available to the Commission in such actions—as well as the Commission's well-documented higher rate of prevailing before its ALJs. This expansion in the use of proceedings over which ALJs preside—and the contemporaneous expansion in ALJs' powers—significantly increases the real-world importance of resolving the issue presented in this case.

A. The Expanded Authority Of SEC ALJs.

Recent statutory changes have expanded both the reach of SEC administrative proceedings and the range of available sanctions.

Originally, the ability of the Commission to use administrative proceedings was limited: The Commission could proceed administratively only against registered entities, and could only obtain a "stop order" to halt an offering of securities to the public, see Securities Act of 1933 § 8, 48 Stat. 74, 79-80, or reject an application for or revoke the registration of a broker-dealer or investment adviser, see Securities Exchange Act of 1934 § 15, 48 Stat. 881, 895-96; Investment Company Act of 1940 § 203, 54 Stat. 789, 850-52.

In the ensuing decades, the powers and jurisdiction of the SEC ALJs expanded, but until 2009, the authority to impose monetary penalties against persons or entities not registered with the Commission remained for the most part with federal district courts. See, e.g., Securities Enforcement Remedies and Penny Stock Reform Act of 1990 §§ 102, 202-203, 301, 401, 104 Stat. 931, 933-35, 937-40, 941-44, 946-49. See also Andrew Ceresney, Dir., SEC Div. of Enforcement, Remarks to the American Bar Association's Business Law Section Fall Meeting (Nov. 21, 2014) ("Ceresney 2014"), http://www.sec.gov/News/Speech/Detail/Speech/1370543515297 ("Until 2010, while we could proceed against unregistered persons in administrative proceedings, the relief that we could obtain against them was limited.").

In 2010, however, with the passage of the Dodd-Frank Act, the Commission gained the power to obtain through administrative proceedings virtually

the same relief—including substantial monetary penalties—against the same individuals and entities that it could sue in federal district court. See Ceresney 2014, *supra* p. 5 ("In the Dodd-Frank Act, * * * Congress provided us authority to obtain penalties in administrative proceedings against unregistered parties comparable to those we already could obtain from registered persons."); Jed S. Rakoff, PLI Secs. Reg. Institute Keynote Address, Is the S.E.C. Becoming a Law Unto Itself? (Nov. 5, 2014), http://assets.law360news.com/0593000/593644/Sec.Reg.Inst.final.pdf ("The net result of all this is that the S.E.C. can today obtain through internal administrative proceedings nearly everything it might obtain by going to court."); Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, § 929P, 124 Stat. 1376, 1862-64.

Now the Commission can proceed administratively against *any* person or entity. See 15 U.S.C. §§ 77h-1, 78u-3(a), 80a-9(f), 80b-3(k). And it can obtain in those proceedings, *inter alia*, monetary and other civil penalties such as fines (including against unregistered persons), see *id.* §§ 77h-1(e), (g), 78u-2, 78u-3(e), 80a-9(d)-(e), 80b-3(i)-(k); cease and desist orders, see *id.* §§ 77h-1, 78u-3(a), 80a-9(f), 80b-3(k); and collateral bars prohibiting individuals from associating with entities regulated by the SEC, see *id.* §§ 78o(b)(6)(A), 78o-4(c)(4), 78q-1(c)(4)(C), 80b-3(f).

B. The Commission's Increasing Use Of In-House Administrative Proceedings.

The expansion of the authority of SEC ALJs has been accompanied by a dramatic increase in the Commission's use of administrative enforcement proceedings as compared to civil actions in court.

That change was deliberate. In October 2013, Andrew Ceresney, then-Director of the Division of Enforcement, expressly signaled the Commission's intention to funnel enforcement actions into administrative proceedings before SEC ALJs as opposed to federal court, stating that "[o]ur expectation is that we will be bringing more administrative proceedings given the recent statutory changes." Gretchen Morgenson, *At the S.E.C., a Question of Home-Court Edge*, N.Y. TIMES, Oct. 5, 2013. A year later, he confirmed that "[t]here is no question that we are using the administrative forum more often now than in past years, given the changes under Dodd-Frank." Ceresney 2014, *supra* p.5; see *also* H.R. Rep. No. 114-697, at 2 (2016) ("This shift from litigation in court to administrative proceedings has occurred largely as a result of Section 929P of the [Dodd-Frank] Act, which expanded the SEC's authority to obtain civil penalties in administrative proceedings against any person or entity").

Indeed, "[p]ublicly available data indicate that in FY 2014, the SEC's Enforcement Division brought nearly half of its litigated actions as administrative proceedings, *an increase of over 35% since 2012*." H.R. Rep. No. 114-697, at 2 (emphasis added). And the trend toward administrative proceedings has continued: In fiscal year 2016, the percentage of enforcement actions brought as administrative proceedings rose to 80% of all enforcement actions (74% if follow-on administrative proceedings are excluded). SEC, Select SEC and Market Data Fiscal 2016 at 3 tbl. 2, https://www.sec.gov/files/2017-03/secstats2016.pdf; see also H.R. Rep. No. 114-697, at 2-3 ("[I]t has been reported that the SEC brought 82% of its enforcement actions as administrative proceedings, rather than federal-court cases, in the six months

ending in March 2015, representing an increase from less than half of those matters a decade earlier.").[3]

The types of cases presided over by SEC ALJs have changed as well. Prior to the Dodd-Frank Act, for example, the SEC had never brought an insider trading case before an ALJ. Now, however, the SEC regularly brings such cases before ALJs. See SEC, Select SEC and Market Data Fiscal 2016 at 3 tbl. 2; Sarah N. Lynch, *U.S. SEC to File Some Insider-Trading Cases in Its In-House Court*, REUTERS, June 11, 2014, http://www.reuters.com/article/sec-insider trading-idUSL2N0OS1AT20140611.

C. The Commission's Home Court Advantage In Administrative Proceedings.

The Commission's increased use of in-house administrative proceedings before SEC ALJs has one undisputable result: the Commission prevails much more frequently. That materially and adversely affects the rights and interests of businesses and individuals subject to SEC enforcement actions and to SEC regulation more generally. But the absence of the clear responsibility required by the Constitution for the appointment of SEC ALJs clouds accountability for any biases in the administrative process.

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[3] The increase in the share of enforcement actions brought against public companies in administrative proceedings as opposed to in civil court actions is even more dramatic: In those actions, the percentage of enforcement actions brought in administrative proceedings increased from 34% in 2010 to 90% in 2016. NYU Pollack Ctr. for Law & Business, SEC Enforcement Activity Against Public Companies and Their Subsidiaries: Fiscal Year 2016 Update at 6, https://www.cornerstone.com/Publications/Reports/SEC-Enforcement-Activity-Against-Public-Company-Defendants-2016.

The Commission enjoys a higher rate of success in its proceedings before SEC ALJs than in civil court actions. Between October 2010 and March 2015, the SEC won 90% of the cases it brought before its ALJs, as compared with 69% of cases before district court judges. Jean Eaglesham, *SEC Wins With In-House Judges*, WALL ST. J., May 6, 2015, https://www.wsj.com/articles/sec-wins-with-in-house-judges-1430965803. It won *every one* of the 219 administrative decisions issued between October 2013 and January 2015. Ryan Jones, *The Fight Over Home Court: An Analysis of the SEC's Increased Use of Administrative Proceedings*, 68 SMU L. REV. 507, 509 (2015).

Furthermore, administrative proceedings before ALJs differ from federal court cases in several ways that meaningfully impact the ability of defendants to present a full defense. For example, defendants have limited ability to obtain pre-hearing discovery, have a short period of time to prepare for a hearing, are not protected by the evidentiary safeguards of the Federal Rules of Evidence, and have no right to a jury trial. See Joseph A. Grundfest, *Fair or Foul?: SEC Administrative Proceedings and Prospects for Reform Through Removal Legislation*, 85 FORDHAM L. REV. 1143, 1156-65, 1169-74 (2016) ("Grundfest"); see also H.R. Rep. No. 114-697, at 3; U.S. Chamber of Commerce, *Examining U.S. Securities and Exchange Commission Enforcement: Recommendation on Current Processes and Practices* at 14-17 (2015), http://www.centerforcapitalmarkets.com/wp-content/uploads/2015/07/021882_SEC_Reform_FIN1.pdf.

Of course, the SEC may take years to investigate and develop a case, during which time it has essentially unfettered authority to request documents and

interview witnesses. See Grundfest at 1158. The imbalance between the SEC and defendants in administrative proceedings has raised concerns about the fairness of such proceedings, which further underscores the importance of transparency and accountability in the conduct of the proceedings.

Moreover, the real-world impact of decisions by SEC ALJs extends beyond the individual enforcement actions over which the ALJs preside. Agencies, and particularly the SEC, have long used administrative proceedings to establish standards and policies outside of the formal rulemaking process. See David L. Shapiro, *The Choice of Rulemaking or Adjudication in the Development of Administrative Policy*, 78 Harv. L. Rev. 921, 926 (1965); *SEC* v. *Chenery Corp.*, 332 U.S. 194, 201-03 (1947).

The increased use of administrative proceedings accordingly produces a correspondingly greater role for ALJs in agency policymaking. It also transfers responsibility for construing and interpreting the securities laws from federal courts to ALJs because federal courts reviewing administrative decisions defer to ALJs' legal conclusions. See Rakoff at 10-12; Grundfest at 1149, 1165-66. Indeed, the SEC's own internal guidance on forum selection recommends bringing an enforcement action as an administrative proceeding before an in-house ALJ, as opposed to as a civil action in court, if it "is likely to raise unsettled and complex legal issues under the federal securities laws, or interpretation of the Commission's rules." SEC, Division of Enforcement Approach to Forum Selection in Contested Actions at 3, https://www.sec.gov/divisions/enforce/enforcement-approach-forum-selection-contested-actions.pdf.

In view of the increasingly central role of SEC ALJs in adjudicating enforcement actions and shaping the policy and law governing individuals and businesses, it is all the more important that this Court resolve the question whether the Appointments Clause's significant structural safeguards apply to the appointment of those ALJs so that the public can easily discern and hold accountable the individual(s) responsible for their appointment—a question that, as described below, has divided the lower courts.

II. The Petition Cleanly Presents A Circuit Conflict That Is Ripe For Resolution.

In the *per curiam* decision below, an evenly-divided D.C. Circuit rejected petitioners' argument that their petition for review should be granted because SEC ALJs are "Officers" who must be appointed in compliance with the Appointments Clause, leaving in place the opinion of the three-judge panel of the D.C. Circuit holding that lack of final decisionmaking authority by itself disqualifies SEC ALJs from being "Officers" subject to the Appointments Clause.

The Tenth Circuit, in *Bandimere* v. *SEC*, addressed "the same question" as the court below—whether SEC ALJs are "Officers" subject to the Appointments Clause—and reached the opposite conclusion: "SEC ALJs are inferior officers who must be appointed in conformity with the Appointments Clause." 844 F.3d at 1181.

As a result of the circuits' divergent opinions, whether or not businesses and individuals are assured that their rights and interests will be determined by an official appointed according to the dic-

tates of the Appointments Clause depends on their geographic location. The disparate effect on businesses and individuals of this split is already apparent.

The Commission has stayed all administrative proceedings reviewable in the Tenth Circuit. *See* Order, *In re Pending Administrative Proceedings*, Securities Act of 1933 Release No. 10365 (May 22, 2017). But it continues to bring enforcement actions before SEC ALJs against respondents located outside of the Tenth Circuit. *See* U.S. SEC, Administrative Proceedings, https://www.sec.gov/litigation/admin.shtml; *see also* Order Denying Motion to Stay Administrative Proceeding, *In the Matter of Tilton*, Investment Advisers Act of 1940 Release No. 4735 (July 28, 2017).

Moreover, the conflict between these lower courts turns on the proper interpretation of this Court's Appointments Clause precedents—in particular *Freytag* v. *Comm'r*, 501 U.S. 868. The D.C. Circuit panel's decision rested on a severely restrictive interpretation of "Officers" that "begins, and ends" with whether an official has the authority to issue final decisions. Pet. App. 13a. That interpretation was in turn based on the D.C. Circuit's view that the authority to issue final decisions "'was critical to the Court's decision' in *Freytag*" that special trial judges are "Officers." *Id.* 12a.

The Tenth Circuit expressly "disagree[d]" with the D.C Circuit panel's elevation of final decision-making power as the dispositive factor in determining whether an official is an "Officer" for purposes of the Appointments Clause. *Bandimere*, 844 F.3d at 1182. "Whether SEC ALJs can enter final decisions

is not dispositive to our holding because it was not dispositive to *Freytag*'s holding." *Id.* at 1184 n.36.

Only this Court can resolve the conflict. Additional lower court decisions are most unlikely to provide new insights into the meaning of the Court's opinion in *Freytag*. The Court should grant review to resolve the issue and ensure uniform national application of the protections of the Appointments Clause. See *Bullock v. BankChampaign*, N.A., 133 S. Ct. 1754, 1761 (2013) ("[I]t is important to have a uniform interpretation of federal law").

III. The Decision Below Conflicts With This Court's Precedent.

A. The Appointments Clause Applies To All Officials Who Exercise Significant Authority.

This Court has consistently recognized that the Appointments Clause of the U.S. Constitution has "substantive meaning" and for good reason. *Buckley v. Valeo*, 424 U.S. 1, 126 (1976). The Constitution's separation of powers, with its attendant checks and balances, is "essential to the preservation of liberty," and also ensures that "[a] dependence on the people" is the "primary control on the government." THE FEDERALIST NO. 51, at 261-262 (James Madison) (Garry Wills ed., 1982).

The Framers recognized that when the appointment power is dispersed among multiple people, "[s]candalous appointments to important offices" are made, and it is impossible to "determine by whose influence [the people's] interests have been committed to hands so unqualified, and so manifestly improper." THE FEDERALIST NO. 70 at 359 (Alexander Hamilton). The Constitution therefore "carefully hus-

band[s] the appointment power to limit its diffusion," *Freytag*, 501 U.S. at 883, and thus permits the people to "determine what part had been performed by the different actors," THE FEDERALIST NO. 77 at 389 (Alexander Hamilton). With respect to "inferior Officers," the Appointments Clause grants Congress "only limited authority to devolve appointment power on the President, his heads of departments, and the courts of law." *Freytag*, 501 U.S. at 884. The Clause thereby ensures that those wielding the appointment power are "accountable to political force and the will of the people." *Id.* at 884.

Consistent with this history, the Court has held that "any appointee exercising significant authority pursuant to the laws of the United States" is an "Officer of the United States" who must be appointed in accordance with the terms of the Appointments Clause of the U.S. Constitution. *Buckley*, 424 U.S. at 126; see also *id.* at 132 ("Unless their selection is elsewhere provided for, *all* Officers of the United States are to be appointed in accordance with the Clause." (emphasis added)); *Freytag*, 501 U.S. at 881.

The class of officials covered by the Clause has been described as "unusually broad," and including among others a district court clerk, the "thousands of clerks in the Departments of the Treasury, Interior and the othe[r] departments," a "clerk to the assistant treasurer stationed at Boston," an "assistant-surgeon," and a "cadet-engineer." *Free Enter. Fund* v. *Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 539-40 (2010) (Breyer, J., dissenting) (internal quotation marks and citations omitted).

Of particular relevance to SEC ALJs is this Court's holding in *Freytag* that special trial judges of the U.S. Tax Court are "inferior officers" based on

the "significance of the duties and discretion that [they] possess." 501 U.S. at 881-82. The Court relied on the fact that special trial judges "perform more than ministerial tasks"; they "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders," and exercise significant discretion in carrying out those "important functions." *Id.*[4]

Since *Freytag*, the Court has also held—virtually summarily—that military judges are officers subject to the Appointments Clause. See *Edmond* v. *United States*, 520 U.S. 651, 662 (1997); *Weiss* v. *United States*, 510 U.S. 163, 169-70 (1994).

B. SEC ALJs Are "Inferior Officers" Under The Appointments Clause.

The Court's precedents cannot be reconciled with the decision below rejecting petitioners' argument that their petition for review should be granted because SEC ALJs are "Officers" required to be appointed in compliance with the Appointments Clause.

Freytag is dispositive: The authority and discretion of SEC ALJs are indistinguishable from the duties of the special trial judges that the *Freytag* Court found sufficiently "significan[t]" to render special trial judges "officers" under the Appointments Clause. 501 U.S. at 881-82.

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[4] The Court held in the alternative that "[e]ven if the duties of special trial judges" in cases in which they did not have final decision-making authority "were not as significant as [it had] found them to be," the judges' authority to enter final decisions in other cases would suffice to make them "officers." *Id.* at 882.

The SEC has delegated to ALJs responsibility for the "fair and orderly conduct of [administrative] proceedings," 17 C.F.R. § 200.14(a), and thereby empowered the ALJs to "perform more than ministerial tasks," *Freytag*, 501 U.S. at 881.[5] An SEC ALJ has "authority to do all things necessary and appropriate to discharge his or her duties." 17 C.F.R. § 201.111. As the petition explains, that includes, but is not limited to: issuing, revoking, quashing, and modifying subpoenas; receiving evidence and ruling on the admissibility of evidence and offers of proof; regulating the course of a proceeding and the conduct of the parties and their counsel; examining witnesses; ordering and regulating document production and depositions; ruling on all procedural and other motions; sanctioning contemptuous conduct; and preparing an initial decision containing factual findings and legal conclusions, the reasons or basis thereof, and an appropriate order, sanction, and relief. *Id.* §§ 200.14(a), 201.111, 201.180, 201.230, 201.233, 201.360; see also 5 U.S.C. § 557(c). See generally 5 U.S.C. § 556(c).

The ALJ's initial decision is "deemed the action of the [SEC]," unless a party or other person entitled to review files a timely petition for review or the SEC on its own initiative exercises its discretionary right to review. 15 U.S.C. § 78d-1(c); see also 17 C.F.R. § 201.360(d); 5 U.S.C. § 557(b). Even in those cases

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[5] Like the office of special trial judge, the office of SEC ALJ is established by law. The Administrative Procedure Act creates the office of the administrative law judge, and sets forth the ALJ's duty of presiding over adjudicatory hearings. 5 U.S.C. §§ 556, 557; see also *id.* §§ 3105, 5372 (setting forth means of appointment and salary). The federal securities laws, in turn, authorize the SEC to "delegate . . . any of its functions to . . . an administrative law judge." 15 U.S.C. § 78d-1(a).

in which a party appeals the ALJ's decision, the SEC retains discretion to decline to review the ALJ's decision, except in a few specified circumstances. See 17 C.F.R. § 201.411(b). As a practical matter, 90 percent of ALJ initial decisions become final without review by the SEC. See *Bandimere*, 844 F.3d at 1187.

In other words, SEC ALJs "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders."[6] *Freytag*, 501 U.S. at 881-82. And "[i]n the course of carrying out these important functions, the [ALJs] exercise significant discretion." *Id.* at 882. These characteristics, which compelled the Court in *Freytag* to find special trial judges of the Tax Court to be "Officers" subject to the Appointments Clause, likewise compel the conclusion that SEC ALJs are "Officers."

The D.C. Circuit panel rested its contrary decision on its conclusion that these ALJs lack the authority to issue final decisions. Pet. App. 13a.

But *Freytag* squarely *rejected* the argument that "special trial judges may be deemed employee in [certain cases] because they lack authority to enter a final decision." 501 U.S. at 881. That view, the Court held, "ignore[d] the significance of the duties and discretion that special trial judges possess" (*id.*)—which, as explained above, SEC ALJs likewise possess.

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[6] Although SEC ALJs do not have the power to impose fines or imprisonment for contempt, they have the authority to impose other sanctions for contemptuous conduct. See 17 C.F.R. § 201.180.

To be sure, after the Court found that special trial judges were officers based on their role and discretion in regulating the trial process, it went on to set forth a separate and independent basis for finding the judges to be officers. "*Even if* the duties of special trial judges" were not as significant as the Court had just found them to be—and thus not sufficient by themselves to render special trial judges officers—"our conclusion" that special trial judges are inferior officers "would be unchanged" because special trial judges have the authority to enter final decision in some categories of cases. *Id.* at 882 (emphasis added).

That authority, the Court explained, was sufficient to categorize special trial judges as inferior officers in all cases, even if the Court assumed that in some cases the judges had neither final decision-making authority nor other significant duties. *Id.* In other words, *Freytag* stands for the proposition that final decision-making authority in some matters would be sufficient to make an official an "officer" for all purposes, even where his other functions are not "significant." But final decision-making authority in all matters is not necessary for "officer" designation.

Subsequent cases confirm this reading of *Freytag*. In *Weiss* v. *United States*, decided just a few years after *Freytag*, this Court held that military judges qualify as officers subject to the requirements of the Appointments Clause. See 510 U.S. at 170.[7]

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[7] The precise issue in *Weiss* was whether the Appointments Clause requires military officers to obtain a separate appointment before serving as military judges. The Court noted that the parties agreed "rightly so" that the Appointments Clause applied to the military judges. 510 U.S. at 170.

Military judges "rule[] on all legal questions, and instruct[] court-martial members regarding the law and procedures to be followed," and, where the accused elects, decide guilt or innocence and impose sentences. *Id.* at 167-68.

However, "[n]o sentence becomes final until approved by the officer who convened the court-martial," and the judges' factual findings, legal rulings, and sentences are subject to *de novo* review by the Courts of Military Review. *Id.* at 167-68; see also *id.* at 193 (Souter, J., concurring); 10 U.S.C. §§ 864, 866, 869. Notwithstanding the military judges' inability to enter final decisions, the Court held that "because of the authority and responsibilities they possess," military judges "act as 'Officers' of the United States." *Weiss*, 510 U.S. at 169.

Similarly, in *Edmond* v. *United States*, this Court held that judges on the Coast Guard Court of Criminal Appeals[8] are inferior officers for purposes of the Appointments Clause. 520 U.S. at 666. The Court expressly recognized that those judges "have no power to render a final decision on behalf of the United States unless permitted to do so by other Executive officers." *Id.* at 665. Nevertheless, the Court "[did] not dispute that military appellate judges are charged with exercising significant authority on behalf of the United States," which rendered them officers under the Appointments Clause. *Id.* at 662.

Indeed, the Court recognized that being subject to review is inherent to the definition of an "inferior

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[8] The Courts of Military Review were renamed the Courts of Criminal Appeals. *See* National Defense Authorization Act for Fiscal Year 1995, § 924, 108 Stat. 2663, 2831 (1994).

officer," who is subject to the Appointments Clause: "[W]e think it evident that 'inferior officers' are officers whose work is directed and supervised at some level by others who were appointed by Presidential nomination with the advice and consent of the Senate." *Id.* at 663.

Thus, in both *Weiss* and *Edmond*, this Court confirmed that the authority to enter final decisions is relevant to distinguishing *inferior* officers from *principal* officers, not to distinguishing inferior officers from mere employees whose appointments are not subject to the strictures of the Appointments Clause. The decision below cannot be squared with these precedents, and the interpretation of the Clause that it embraced unjustifiably excludes scores of officials with significant influence over the interests of the people from the accountability-preserving protections of the Appointments Clause.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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RECORD AND BRIEFS

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IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, *et al.*,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DC CIRCUIT

BRIEF FOR MARK CUBAN AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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INTEREST OF *AMICUS CURIAE*[1]

Mark Cuban is a successful businessman and investor. He defeated an attempt by the U.S. Securities and Exchange Commission (the "SEC" or "Commission") to sanction him as an "insider trader" based on a defective legal theory and incorrect facts. As a first-hand witness to and victim of SEC overreach, Mr. Cuban has an interest in supporting Petitioners' appeal in this case, and in particular demonstrating that both statutory language and legislative history clearly show that Congress specifically intended that SEC hearings only be held before constitutional officers.

According to its website, "[t]he mission of the U.S. Securities and Exchange Commission is to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation."[2] When the laws are applied inconsistently or the process by which they are enforced is rigged to favor the government, capital formation is impeded because market participants do not have clear rules for understanding their investment risks. Put differently, investment risk from arbitrary and biased securities law enforcement is no less a threat to

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1. Pursuant to this Court's Rule 37.6, counsel for *amicus curiae* certifies that this brief was not authored in whole or in part by counsel for any party and that no person or entity other than *amicus curiae* or his counsel made a monetary contribution intended to fund the preparation or submission of this brief. Pursuant to this Court's Rule 37.2(a), both parties received timely notice of the intent to file this brief and have consented to the filing of this brief.

2. *See What We Do*, U.S. Sec. & Exch. Comm'n., https://www.sec.gov/Article/whatwedo.html (last visited Aug. 25, 2017).

capital formation than investment risk resulting from lax enforcement; they are two sides of the same coin.

As a businessman who has faced down a misguided SEC enforcement litigation, Mr. Cuban has an abiding interest in challenging the SEC when it takes misguided and incorrect positions in litigation. Here, the SEC has done exactly that in claiming that Congress's chosen language is "irrelevant" and that the Commission can ignore legislative intent and delegate to mere employees, rather than to constitutional officers, the power to preside over hearings having a profound effect on peoples' livelihoods, reputations, and finances.

SUMMARY OF ARGUMENT

The *Lucia* panel not only misapplied *Freytag*'s test for determining whether an individual is required to be a constitutional officer, but also incorrectly dismissed clear congressional intent that SEC administrative law judges ("ALJs") be constitutional officers. *See Raymond J. Lucia Co., Inc. v. SEC*, 832 F.3d 277, 289 (2016), *aff'd en banc by an equally divided court*, 2017 WL 2727019 (D.C. Cir. June 26, 2017). This *amicus* brief focuses on the second of those defects in the panel decision because the use of the word "officer" in the relevant provisions of the securities laws, the plain wording of the relevant provisions of the Administrative Procedure Act ("APA"), as well as their respective legislative histories, all manifest congressional intent that Commission hearings be held by officers of the United States only. In other words, the Court should grant the Petition for Writ of Certiorari here because the panel's decision thwarts clearly expressed congressional language, understanding, and intent. Of course, as

Petitioners point out, the Petition should be granted because it also misapplies this Court's long-standing, uninterrupted precedent and, until recently, the Executive Branch's own view. *See* Petition for Writ of Certiorari at 18-19, *Lucia v. SEC*, No. 17-130 (July 21, 2017).

The *Lucia* panel erred when it summarily dismissed the language of the federal securities laws commanding that hearings be held before the Commission or "*an officer or officers of the Commission designated by it*," *see, e.g.*, 15 U.S.C. § 77u (emphasis added), by adopting the SEC's formulation that "there is no indication Congress intended these officers to be synonymous with 'Officers of the United States.'" *Raymond J. Lucia Co., Inc.*, 832 F.3d at 289; *see also*, Opinion of the Commission, *In re Raymond J. Lucia Co., Inc.*, Admin. Proc. File No. 3-15006, 2015 WL 5172953, at *23 n.122 (Sept. 3, 2015). The deliberate use of the words "officer or officers" is, of course, one such indication because the word "officer" is imbued with constitutional meaning. The relevant legislative history is another. Yet, the panel was silent in response to Mr. Cuban's statutory interpretation points, as well as his analysis of the legislative history demonstrating that Congress meant and understood that the terms "constitutional officers" and "officers" were synonyms.

The panel's finding of no evidence of congressional intent "that the ALJ who presides at an enforcement proceedings [sic] be delegated the sovereign power of the Commission to *make the final decision*," *Raymond J. Lucia Co., Inc.*, 832 F.3d at 287 (emphasis added), is beside the point, for it confuses *what* may be delegated with *to whom*. It is clear from the legislative history that Congress's intent was not dependent on delegation

of power to issue final decisions; Congress required that hearings be held by constitutional officers because of the seriousness of the subject matter as well as the powers attendant to conducting them (and even gathering evidence in advance of them). To allow the SEC to delegate its hearing powers, or any subset of them, to someone who is not an officer would thwart that plain congressional intent.

In short, when the securities laws and APA are read together, both the statutes and the legislative histories show that while Congress did allow for the possibility that not all ALJs had to be "officers," it clearly intended that SEC ALJs did.

ARGUMENT

I. THE SECURITIES LAWS REQUIRE THAT OFFICERS HOLD SEC HEARINGS.

Congress chose the following language to authorize SEC hearings:

> All hearings shall be public and may be held before the Commission or ***an officer or officers of the Commission designated by it*** . . . .

Securities Act of 1933, 15 U.S.C. § 77u (emphasis added).[3]

3. *See also* Securities Exchange Act of 1934, 15 U.S.C. § 78v ("Hearings . . . may be held before the Commission, any member or members thereof, or any officer or officers of the Commission designated by it . . . ."); Investment Advisers Act of 1940, 15 U.S.C. § 80b-12 (same); Investment Company Act of 1940, 15 U.S.C. § 80a-40 (same).

Plain language of legislation must be given its plain meaning. *Hardt v. Reliance Standard Life Ins. Co.*, 560 U.S. 242, 251 (2010) ("[W]e begin by analyzing the statutory language . . . . We must enforce plain and unambiguous statutory language according to its terms." (citations omitted)); *United States v. Germaine*, 99 U.S. 508, 510 (1878) (finding that when Congress uses the phrase "officers of the United States," it means "constitutional officers" and stating that an intent to describe someone other than a constitutional officer is denoted by words such as "servant, agent, person in the service or employment of the government"). Unless contrary intent is apparent, in other words, one must assume that Congress meant "officers" in the constitutional sense when it used the word "officers" for at least three reasons. First, the word "officer" is imbued with significant meaning in our constitutional framework—Article II, Section 2 of the Constitution itself refers to the "principal Officer in each of the executive Departments," "Officers of the United States," and "inferior Officers." U.S. Const. art. II, § 2; *see Buckley v. Valeo*, 424 U.S. 1, 125-26 (1976). Second, because this Court has expressly interpreted the phrase "officer of the United States" in legislation as meaning "constitutional officer." *See Germaine*, 99 U.S. at 510; *see also Jerman v. Carlisle, McNellie, Rini, Kramer & Ulrich LPA*, 559 U.S. 573, 589-90 (2010) ("[W]hen 'judicial interpretations have settled the meaning of an existing statutory provision, repetition of the same language in a new statute indicates, as a general matter, the intent to incorporate its . . . judicial interpretations as well.'" (citations omitted)). And third, the grouping of the Commission itself with its officers in this provision implies a parity of stature—*i.e.*, this is a reference to constitutional officers because they are empowered to "exercis[e] significant authority pursuant to the laws of the

United States." *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 486 (2010) (quoting *Buckley*, 424 U.S. at 125-26).

II. LEGISLATIVE HISTORY OF THE RELEVANT STATUTES CONFIRMS THE PLAIN LANGUAGE—CONGRESS INTENDED TO DELEGATE EXECUTIVE POWER TO CONSTITUTIONAL OFFICERS.

Even if there were some ambiguity to Congress's chosen language justifying a search for intent, the relevant legislative history demonstrates Congress's intent that SEC hearings be held before constitutional officers.

A. The Legislative History of the Securities Act.

Congressional debate in connection with the House bill that eventually became the Securities Act of 1933 reflects deep concerns about vesting with any non-judicial officer the power to hold hearings, administer oaths and affirmations, compel attendance, and recommend severe sanctions. Indeed, initially there was even dissension as to whether the Commission itself and any of its members—all principal officers—should hold this power.

A predecessor provision to Sections 20 and 21 in the initial House draft would have authorized the Commission (then the Federal Trade Commission) to revoke a company's registration if, among other things, it found that the company was in unsound condition. H.R. 4314, 73d Cong. § 6 (1933).[4] Certain members of Congress expressed

4. The current provision for Cease-and-Desist Proceedings appears at 15 U.S.C. § 77h-1; the current provision for Injunctions

concern that the power to take away someone's business because it was "unsound" was both unprecedented and immense. *See, e.g., Federal Securities Act: Hearing Before the H. Comm. on Interstate and Foreign Commerce*, 73d Cong. 45 (1933) (Representative Clarence Lea described this power as "a rather radically different field" than the one of controlling publicity or disclosures).

To address these concerns, drafters initially proposed vesting such powers only in *principal* officers of the United States. For example, an early draft bill, H.R. 4314, placed officers empowered to act for the Commission on the same footing as Commission members who were principal officers:

> SEC. 6. That the Commission may revoke the registration of any security by entering an order to that effect . . . . In making such examination ***the Commission or other officer or officers designated by it*** shall have access to and may compel the production of all the books and papers of such issuers . . . and may administer oaths to and examine the officers of such issuers . . . and may, in its discretion, require the production of a balance sheet exhibiting the assets and liabilities . . . .

H.R. 4314, 73d Cong. § 6 (1933) (emphasis added). Initial drafts of this legislation always contemplated that

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and Prosecution of Offenses appears at 15 U.S.C. § 77t; and the current provision for Hearings by Commission appears at 15 U.S.C. § 77u.

members of the Commission would be principal officers.[5] Therefore, the use of the word "other" to modify the words "officer or officers" suggests parity; reflecting congressional intent that investigations and hearings be conducted either by principal officers who are Commissioners or other principal officers designated by the Commission for that purpose.

Congress was concerned about vesting this amount of control and power *even* with principal officers. In one illuminating exchange during the hearings, the Chairman of the relevant House Committee questioned whether *any* administrative officer of the government should have that much power. *Federal Securities Act: Hearing Before the H. Comm. on Interstate and Foreign Commerce*, 73d Cong. 135 (1933) (statement of Rep. Sam Rayburn, Chairman, H. Comm. on Interstate and Foreign Commerce) ("Do you believe that an administrative officer of the Government ought to be given that much power, as a general principle—to pass upon whether or not a man's business is based on sound principles? . . . [B]ut the question that this committee has got to determine is whether or not they want to give anybody that kind of authority."). This concern was echoed at various times throughout the House and Senate Committee hearings. *See, e.g., id.* at 135-36 ("And yet we are committing [these powers] into the hands of a commission, of men appointed by the President, and, of course, confirmed by the Senate. But you know, . . . a board or a commission, is just about as good in its administration, or as bad, as the personnel of the commission."); *Securities Act: Hearings Before the S. Comm. on Banking and Currency*, 73d Cong. 104 (1933)

5. That Commission is "composed of five Commissioners, who shall be appointed by the President, by and with the advice and consent of the Senate." 15 U.S.C. § 41.

(statement of Sen. James F. Byrnes, Member, S. Comm. on Banking and Currency) ("That is quite a lot of power to give to an official, to determine that in his opinion a given enterprise is not based upon sound principles.").

Similarly, a related draft provision authorizing investigations and giving powers to compel production of evidence and take sworn testimony provided:

> For the purpose of all investigations . . . , ***the Commission and officer or officers designated by it*** are empowered to subpena [sic] witnesses, examine them under oath, and require the production of any books, papers, or other documents which the Commission deems relevant or material to the inquiry.

H.R. 4314, 73d Cong. § 15(b) (1933) (emphasis added).[6] Given the revocation-for-being-unsound debate context, the only reasonable interpretation of this language is that it too referred to constitutional officers.

A later draft bill, H.R. 5480, narrowed Section 6 and removed the power to revoke registration of securities based on an unsound condition of an issuer. *See* H.R. 5480, 73d Cong. § 6 (1933). It allowed the Commission to enter a stop order suspending a registration statement if it appeared that the statement included any material false statements or omissions. *Id.* § 8(d). Additionally, it slightly modified the language regarding who was authorized to conduct stop order examinations by replacing the words "other officer" with the words "any officer." *Compare*

6. The current provision states, in relevant part: "[A]ny member of the Commission or any officer or officers designated by it . . . ." 15 U.S.C. § 77s(c).

H.R. 4314, 73d Cong. § 6 (1933) *with* H.R. 5480, 73d Cong. § 8(e) (1933).

This modification shows two things: First, by replacing the word "other" with the word "any," the new draft provision empowered both inferior and principal officers. One can infer that once the drafters narrowed the grounds on which the Commission could revoke a registration, they were comfortable permitting inferior officers to hold examinations and exercise attendant powers. Second, this is a deliberate, considered change because it obviously changes the meaning of the provision. H.R. 5480 was passed on May 5, 1933. 77 Cong. Rec. 2910-55 (1933).

The original Senate draft bill, S. 875, largely tracked the original House bill, H.R. 4314; it too included a clause that would have allowed revocation of a registration of an "unsound" business. *See* S. 875, 73d Cong. § 6(e) (1933). However, the Senate passed a modified version of H.R. 5480. 77 Cong. Rec. 2978-84, 2986-3000 (1933). The differences between the two chambers' bills were reconciled in a Conference Report, and the final public law had three key parts:

> (1) It retained the language in H.R. 5480 regarding the powers of "***the Commission or any officer or officers designated by it***" to examine witnesses under oath and require the production of documents in connection with a stop order examination, *id.* at 3894 (emphasis added);[7]

7. The relevant language remains materially the same today. *See* 15 U.S.C. § 77h(e).

(2) It modified the language of H.R. 5480 regarding investigations, so that "***any member of the Commission or any officer or officers designated by it*** are empowered to administer oaths and affirmations, subpena [sic] witnesses, take evidence, and require the production" of documents for purposes of investigations, 77 Cong. Rec. 3896 (1933) (emphasis added);[8] and

(3) It added a section entitled "Hearings by Commission," directing that: "All hearings shall be public and may be held before ***the Commission or an officer or officers of the Commission designated by it*** . . . ," 77 Cong. Rec. 3896-97 (1933) (emphasis added).

The Conference Report was subsequently agreed to by both the House and Senate. *Id.* at 3903, 4009 (1933).

In sum, Congress chose the word "officer" carefully and calibrated its grant of authority to executive officers based on the scope of delegated powers.

B. The Legislative History of the Securities Exchange Act.

The following year, Congress passed a companion act, the Securities Exchange Act of 1934. This act, of course,

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8. Note that "and" was replaced with "or," resulting in "the Commission ***or*** any officer or officers," and indicating that Congress was focused on this provision. *Compare* H.R. 4314, 73d Cong. § 15(b) (1933) *with* 77 Cong. Rec. 3896 (1933).

set up the SEC. In it, Congress imbued the Commission and the officers it designated with certain executive functions, such as subpoenaing witnesses, administering oaths, and compelling the production of documents.

Notably, the initial version of the Senate bill included much of the same language and structure as the Securities Act on the relevant issues. That draft started by outlining the "Special Powers of the Commission" in Section 18:

> For the purpose of all investigations which, in the opinion of the Commission, are necessary and proper for the enforcement of this Act, ***any member of the Commission or any officer or officers designated by it are empowered to administer oaths and affirmations, subpena [sic] witnesses, compel their attendance, take evidence, and require the production of*** any books . . . .

S. 2693, 73d Cong. § 18(e) (1934) (emphasis added). As with the Securities Act, this was a grant of executive power to the Commission members and any officers designated by the Commission (and no one else).[9]

The attention to the wording of the provision authorizing hearings in the Exchange Act further indicates that Congress intended hearings to be held by constitutional officers. The draft provided: "All hearings shall be public and may be held before the Commission, ***any member or members thereof*** or an officer or officers of the Commission designated by it, and appropriate records thereof shall be kept." S. 2693, 73d Cong. § 21 (1934)

9. The relevant language remains materially the same today. *See* 15 U.S.C. § 78u(b).

(emphasis added). Note that the highlighted language was an addition to the language in the Securities Act's analogous provision, making it even more explicit that not all hearing officers needed to be principal officers, *i.e.*, Commission members. Apparently, having resolved (with the Securities Act's passage) that inferior officers could also hold hearings, Congress added the highlighted language to reflect that. In short, Congress chose carefully who could wield the hearing-related powers it was delegating. That careful choice would be upended were one to read "employee" where Congress said "officer."

Finally, Congress understood that the choice of the words "employee" or "officer" in the Exchange Act carried legal implications. For example, the use of the word "appoint" in Section 4, which establishes the Commission and authorizes it to employ staff, indicates that Congress was sensitive to the significance of the term "officer."[10] Specifically, initial House and Senate drafts did not authorize the Commission to "appoint" officers or anyone else. *See, e.g.*, H.R. 7924, 73d Cong. § 3 (1934); S. 2642, 73d Cong. § 4(e) (1934) (initial Senate draft: "The Commission is further authorized, in accordance with the civil service laws, to employ . . . such officers and employees . . . as may be necessary . . . ."). The addition of the word "appoint" in the enacted law signified that Congress understood that the Commission needed authority to appoint "officers."[11]

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10. Section 4(b) of the final enacted law reads, in relevant part: "The Commission is authorized to appoint and fix the compensation of such officers, attorneys, examiners, and other experts as may be necessary . . . and the Commission may . . . appoint such other officers and employees as are necessary . . . ." S. 875, 73d Cong. § 4(b) (1933).

11. The current provision is: "The Commission shall appoint and compensate officers, attorneys, economists, examiners, and

C. The Legislative History of the APA.

The plain language and legislative history of the APA also clearly indicate congressional intent that SEC ALJs be inferior constitutional officers. In fact, under the APA, Congress determined the method for appointing ALJs—following lengthy discussions and analysis—with the constraints of the Appointments Clause in mind, *i.e.*, that certain of the ALJs would be "inferior Officers."

1. The APA places ALJs on the same footing with principal officers.

In parallel with the placement of hearing officers on par with the Commission members in the securities laws, the APA also places ALJs on par with heads of departments, *i.e.*, principal officers; to wit: "There shall preside at the taking of evidence—(1) the agency; (2) one or more members of the body which comprises the agency; or (3) one or more administrative law judges appointed under section 3105 of this title." 5 U.S.C. § 556(b).[12] As the discussion below shows, this was no accident; this

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other employees in accordance with section 4802 of title 5." 15 U.S.C. § 78d(b)(1).

12. In 1978, Congress amended the United States Code to change the title of "hearing examiners" to "Administrative Law Judges" and to increase the number of such positions at the GS-16 level. Act of Mar. 27, 1978, Pub. L. No. 95-251, 92 Stat. 183, 183-84 (reclassifying hearing officers as administrative law judges). Before this public law was enacted, the Senate Committee on Governmental Affairs issued a Senate Committee Report explaining that "individuals appointed as ALJ's [sic] hold a position with tenure very similar to that provided for Federal judges under the Constitution." S. Rep. No. 95-697, at 2 (1978).

language reflects Congress's policy choices and careful analysis.

2. Empowerment of ALJs was a reaction to earlier functioning of administrative agencies.

The APA stemmed from a review of administrative agencies following the expansion of the administrative state after the Great Depression. A report by the Attorney General's Committee on Administrative Procedures outlined certain procedural and substantive defects in the then-current administrative functions, including in formal adjudications, and provided a proposed draft of the APA. *See* Attorney Gen.'s Comm. on Admin. Procedure, Letter of Transmittal of Final Report (1941); *see generally* Attorney Gen.'s Comm. on Admin. Procedure, Final Report (1941). The concerns raised in the report animated the passage of the APA and informed much of its language.

The Committee recommended that:

- Agency heads delegate much of the investigatory and prosecutorial functions to capable officers and the initial adjudicative functions to other independent officers. Attorney Gen.'s Comm. on Admin. Procedure, Final Report 55-57 (1941).

- The status of all hearing officers be elevated to allow them to exercise independent and executive functions. *Id.* at 43-44, 46.

- The hearing officers' initial decisions be given real weight, *i.e.*, the initial decision would become final absent clear error. *Id.* at 51.

- Congress empower the hearing officers to exercise certain executive or sovereign functions, such as "preside at hearings, issue subpoenas, administer oaths, rule upon motions, carry out other duties incident to the proper conduct of hearings, and make findings of fact, conclusions of law, and orders for the disposition of matters coming before them." *Id.* at 50.

- An independent body be in charge of approving candidates to ensure that they are well qualified, noting "the hearing commissioner is in a very real sense acting for the head of the agency." *Id.* at 47.

3. Congress intended ALJs to be "presiding officers," appointed in accordance with the Appointments Clause.

Acting on the above-described prescriptions, Congress passed the APA, which, as detailed below: (1) made the hearing examiners "presiding officers"; (2) granted them certain executive powers; (3) mandated that the decisions of subordinate officers be given weight and force; and (4) made certain that the appointment of ALJs are made in conformity with the Appointments Clause.

(i) Congress referred to hearing examiners as "presiding officers."

To start, Congress referred to hearing examiners as "presiding officers" in the original legislation, to wit:

> ***Presiding officers.***—There shall preside at the taking of evidence (1) the agency, (2) one or

> more members of the body which comprises the agency, or (3) one or more examiners appointed as provided in this Act; . . . The ***functions of all presiding officers and of officers participating in decisions*** in conformity with section 8 shall be conducted in an impartial manner.

Administrative Procedure Act of 1946, Pub. L. No. 79-404, § 7(a), 60 Stat. 237 (1946) (emphasis added). Parallel to the Exchange Act, this provision covered three categories of persons: the Commission acting together, individual Commissioners, and other persons appointed to hold the hearing. The words "the functions of all presiding officers" referred to all three of these categories. The sole sensible reading of this language is that the grouping of examiners with principal officers in this section indicates the elevation of examiners to officer status.

The very next provision of the APA as originally adopted supports this reading. It states:

> ***Hearing powers.—Officers presiding at hearings shall have authority***, subject to the published rules of the agency and within its powers, to (1) administer oaths and affirmations, (2) issue subpenas [sic], . . . and (9) take any other action authorized by agency rule consistent with this Act.

Id. § 7(b) (emphasis added). Moreover, that "hearing examiners" were given the same powers as principal officers of the United States is yet another indication that Congress intended delegation of sovereign powers, rendering them inferior officers.

(ii) The statutory definitions of "officer" and "employee" confirm that Congress intended SEC ALJs to be "inferior officers."

In 1965, in connection with the adoption of the revised Title 5, Congress restated "in comprehensive form, without substantive change, the statutes in effect before July 1, 1965, that relate to Government employees, the organization and powers of Federal agencies generally, and administrative procedure . . . ." H. R. Rep. No. 89-901, at 1 (1965). In short, Congress made language changes to streamline and standardize terms across various interrelated statutory provisions without changing their meaning. *Id.* at 2-3.[13]

Among other things, Congress defined the terms "officer" and "employee" in new Sections 2104 and 2105, respectively. *See generally id.* at 8, 10, 12-13. Applying these definitions, Congress amended the hearing-authorizing provisions of the APA thus:

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13. The House Judiciary Committee's Report accompanying these language changes provides, in relevant part:

> ***Substantive change not intended.***—Like other recent codifications undertaken as a part of the program of the Committee on the Judiciary of the House of Representatives to enact into law all 50 titles of the United States Code, there are no substantive changes made by this bill enacting title 5 into law. . . . In a codification statute, [courts presume that] the statute is intended to remain substantively unchanged.

Id. at 3.

> The words "employee" and "employees" [were] substituted [in Section 556(b)] for "officer" and "officers" ***in view of the definition of "employee" in section 2105***. The sentence "A presiding or participating employee may at any time disqualify himself[,]" is substituted for the words "Any such officer may at any time withdraw if he deems himself disqualified."

Id. at 13 (emphasis added).

Similar changes and qualifying comments were made in Section 557. *Id.* By noting that the substitution of "employee" for "officer" was made in view of the expansive definition of "employee," Congress indicated that it understood that "officer" and "employee" were not interchangeable terms and that, therefore, as originally drafted, officer did not mean employee. *See id.* An analysis of these definitions shows that SEC ALJs are officers under the APA.

"Officer" is defined thus:

> (a) For the purpose of this title, "officer", except as otherwise provided by this section or when specifically modified, means a justice or judge of the United States and ***an individual who is***—
>
> > (1) ***required by law to be appointed*** in the civil service ***by*** one of the following acting in an official capacity—
> >
> > > (A) the President;
> > > (B) a court of the United States;

(C) ***the head of an Executive agency***; or
(D) the Secretary of a military department;

(2) engaged in the performance of a Federal function under authority of law or an Executive act; and

(3) subject to the supervision of an authority named by paragraph (1) of this section, or the Judicial Conference of the United States, while engaged in the performance of the duties of his office.

5 U.S.C. § 2104 (emphasis added).

"Employee" is defined thus:

(a) For the purpose of this title, "employee", except as otherwise provided by this section or when specifically modified, ***means an officer*** and an individual who is—

(1) appointed in the civil service by one of the following acting in an official capacity—

(A) the President;
(B) a Member or Members of Congress, or the Congress;
(C) a member of a uniformed service;

> (D) an individual who is an employee under this section;
> (E) the head of a Government controlled corporation; or
> (F) an adjutant general designated by the Secretary concerned under section 709(c) of title 32;
>
> (2) engaged in the performance of a Federal function under authority of law or an Executive act; and
>
> (3) subject to the supervision of an individual named by paragraph (1) of this subsection while engaged in the performance of the duties of his position.

5 U.S.C. § 2105 (emphasis added). In other words, the definition automatically includes all officers (both principal and inferior) as well as certain non-officers falling within subsections (a)(1), (a)(2), and (a)(3).

SEC ALJs meet the statutory definition of "employee" in Section 2105 solely because they meet the statutory definition of "officer" in Section 2104. SEC ALJs are not covered by subsections (a)(1) and (a)(3) of Section 2105 because they must be designated by the Commission under the securities laws (as discussed above) and, under the APA, they must be appointed by the "agency." *See* 5 U.S.C. § 3105 ("Each agency shall appoint as many administrative law judges as are necessary for proceedings required to be conducted in accordance with sections 556 and 557 of this title."). In other words, SEC ALJs do not meet Section

2105's tests for non-officer employees. But, SEC ALJs are "officers" under Section 2104 because they (1) must be appointed by the Commission; (2) perform their duties under authority of law; and (3) are subject to supervision by the head of an executive agency—the Commission.[14] Accordingly, because they are officers under Section 2104, they also are "employees" under the preambular language of Section 2105(a).

4. Congress explicitly made certain that ALJs' appointment complied with the Appointments Clause.

The Attorney General's Committee Report recommended that hearing officers be appointed by an independent government body. Attorney Gen.'s Comm. on Admin. Procedure, Final Report 47-48 (1941). To accomplish this, the Committee recommended the formation of an "Office of Administrative Justice," whose Director would be appointed by the Judicial Conference and who would, in turn, appoint hearing examiners. S. Doc. No. 79-248, at 41-42 (1944-46).

This proposal was rejected because it ran afoul of the Appointments Clause. As explained by the Senate Judiciary Committee:

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14. The word "agency" refers to the entire body that comprises the agency, *i.e.*, all Commissioners acting together as a Commission. The Commission acting together is the head of the agency. *See* Opinion of the Commission, *In re Timbervest, LLC*, Admin. Proc. File No. 3-15519, 2015 WL 5472520, at *23 n.137 (Sept. 17, 2015) ("The Commission constitutes the 'head of a department' when its commissioners act collectively." (quoting *Free Enter. Fund*, 561 U.S. at 512-13)). "Agency" is, therefore, another term for the agency head.

> The legal difficulty with the suggestion, however, is that the ***Constitution provides for the placing of powers of appointment*** "in the courts of law" whereas the Judicial Conference is a committee and not a court and hence may ***not be within the constitutional authorization for appointing powers***.

Id. at 42 (emphasis added).

The same concerns were voiced in the House hearings. The then-President of the American Bar Association ("ABA") testified as follows:

> Third is a suggestion that the Judicial Conference appoint an officer to appoint and remove examiners. This suggestion is attractive, but may present constitutional problems as to the appointing power. Perhaps a solution would be for the Presidential appointment of such an officer or officers, with provision for the Judicial Conference to make recommendations to the President.

Id. at 50. The very next suggestion taken up (and ultimately adopted) by the Senate Judiciary Committee was that the "examiners be appointed '***by*** each agency' rather than [just] 'for each agency.'" *Id.* at 42. In those instances where agency heads are heads of departments, such as the SEC, this change ensured proper Article II appointments.

5. Congress was conferring significant executive powers in the APA.

Were Congress not conferring significant executive powers on ALJs, it would not have bothered with the Appointments Clause. The following comment from the Senate Judiciary Committee is illuminating:

> It has been suggested that this bill should grant the subpena [sic] power to all hearing officers, ***whether or not the agency has been granted such power.*** It may seem logical that hearing officers should have compulsory process powers, but it has been felt that the grant of such powers is of such a nature and so important as to be better left to Congress in connection with specific legislation rather than dealt with by a general statute.

Id. at 29-30 (emphasis added). There would be no reason to consider giving ALJs *independent* subpoena powers if Congress meant them to be mere employees whose job was limited to serving as aides to the Commission. Note that the decision not to vest ALJs with independent subpoena power did not rest on their status as mere employees or aides. Rather, Congress saw the delegation of subpoena power to be significant enough to require a specific statutory grant. *A fortiori*, the grant of subpoena powers to SEC ALJs is a delegation of significant executive power.

To be sure, the original APA text distinguished between supervising officers and subordinate officers, but that distinction is most naturally read as tracking the Constitution's distinction between principal and inferior

officers, because every inferior officer, by definition, is subordinate to, and is subject to supervision by, a principal officer. In referring to subordinate examiners, therefore, Congress repeatedly used the word "officer":

> ACTION BY SUBORDINATES.—In cases in which the agency has not presided at the reception of the evidence, ***the officer who presided*** (or, in cases not subject to subsection (c) of section 5, ***any other officer or officers*** qualified to preside at hearings pursuant to section 7) shall initially decide the case or the agency shall require . . . the entire record to be certified to it for initial decision. Whenever ***such officers*** make the initial decision and in the absence of either an appeal to the agency or review upon motion of the agency within time provided by rule, such decision shall without further proceedings then become the decision of the agency. On appeal from or review of the initial decisions ***of such officers*** . . . . Whenever the agency makes the initial decision without having presided at the reception of the evidence, ***such officers*** . . . .

Administrative Procedure Act of 1946 § 8(a) (emphasis added). It is hard to fathom what Congress could have meant here if not that the persons conducting hearings were constitutional officers—*i.e.*, Commission members who are subordinates for this purpose or their subordinates, inferior officers.

In short, Congress empowered ALJs carefully and in full recognition of the importance of officer status to their functions. As the Senate Judiciary Committee explained,

the APA was "designed to assure that the presiding officer will perform a real function rather than serve merely as a notary or policeman." S. Doc. No. 79-248, at 207, 269.

CONCLUSION

For the foregoing reasons, the Court should grant Petitioners' Petition for Writ of Certiorari.

Respectfully submitted,

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ECORD
AND
RIEF

No. 17-130

In the Supreme Court of the United States

RAYMOND J. LUCIA, et al.,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF AMICUS CURIAE OF PACIFIC LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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IDENTITY AND INTEREST OF AMICUS CURIAE[1]

Founded in 1973, Pacific Legal Foundation is a nonprofit, tax-exempt corporation organized under the laws of the State of California for the purpose of engaging in litigation in matters affecting the public interest. PLF provides a voice in the courts for mainstream Americans who believe in limited government, private property rights, individual freedom, and free enterprise.

PLF is the most experienced public interest legal organization defending the constitutional principle of separation of powers in the arena of administrative law. PLF's attorneys have participated as lead counsel or counsel for amici in several cases before this Court involving the role of the Article III courts as an independent check on the Executive and Legislative Branches under the Constitution's Separation of Powers. *See, e.g.*, *Rothe Dev., Inc. v. Dep't of Def.*, No. 16-1239 (U.S. filed Apr. 13, 2017) (amici's arguing against Executive Branch's unaccountable use of legislative power); *Foster v. Vilsack*, 820 F.3d 330 (8th Cir. 2016), *cert. denied*, 137 S. Ct. 620 (2017) (*Auer* deference to agency staff testimony); *Nat'l Ass'n of Mfrs. v. Dep't of Def.*, No. 16-299 (U.S. filed Sept. 2,

---

[1] Pursuant to this Court's Rule 37.2(a), all parties have consented to the filing of this brief. Counsel of record for all parties received notice at least 10 days prior to the due date of the Amicus Curiae's intention to file this brief. Letters evidencing such consent have been filed with the Clerk of the Court.

Pursuant to Rule 37.6, Amicus Curiae affirms that no counsel for any party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than Amicus Curiae, its members, or its counsel made a monetary contribution to its preparation or submission.

2016) (interpretation of Clean Water Act venue statute); *Gloucester Cnty. Sch. Bd. v. G.G. ex rel. Grimm*, 136 S. Ct. 2442 (2016) (*Auer* deference to agency guidance letter); *U.S. Army Corps of Eng'rs v. Hawkes Co., Inc.*, 136 S. Ct. 1807 (2016) (judicial review of agency interpretation of Clean Water Act); *Decker v. Nw. Envtl. Def. Ctr.*, 133 S. Ct. 1326 (2013) (*Auer* deference to Clean Water Act regulations); *Sackett v. EPA*, 566 U.S. 120 (2012) (same); *Rapanos v. United States*, 547 U.S. 715 (2006) (agency regulations defining "waters of the United States").

PLF supports this petition because it raises core Separation of Powers issues related to each co-equal branch's accountability for the exercise of its powers. PLF's policy perspectives and litigation experience offer an additional viewpoint that will assist the Court in reviewing this petition.

INTRODUCTION AND SUMMARY OF ARGUMENT

This Court has consistently reaffirmed the central judgment of the Framers that the "ultimate purpose of th[e] separation of powers is to protect the liberty and security of the governed." *Metro. Wash. Airports Auth. v. Citizens for the Abatement of Aircraft Noise, Inc.*, 501 U.S. 252, 272 (1991). Indeed, "[n]o political truth is certainly of greater intrinsic value or is stamped with the authority of more enlightened patrons of liberty." *The Federalist No. 47*, at 324 (Madison) (J. Cooke ed. 1961).

Therefore, the liberty and security of the governed are threatened when the carefully balanced scheme of the Framers is not enforced.

In particular here, the question of whether SEC administrative law judges are Officers of the United

States within the meaning of the Appointments Clause implicates the important principle that government must be accountable to the governed. *See Edmond v. United States*, 520 U.S. 651, 660 (1997) ("By requiring the joint participation of the President and the Senate, the Appointments Clause was designed to ensure public accountability for both the making of a bad appointment and the rejection of a good one."); *Freytag v. Comm'r of Internal Revenue*, 501 U.S. 868, 878 (1991) ("The Appointments Clause not only guards against this encroachment [of one branch at the expense of the others] but also preserves another aspect of the Constitution's structural integrity by preventing the diffusion of the appointment power."); Elena Kagan, *Presidential Administration*, 114 Harv. L. Rev. 2245, 2332 (2001) ("The lines of responsibility should be stark and clear, so that the exercise of power can be comprehensible, transparent to the gaze of the citizen subject to it.") (internal quotation marks and citation omitted). *Cf. Dep't of Transp. v. Ass'n of Am. R.R.s*, 135 S. Ct. 1225, 1234 (2015) (Alito, J., concurring) ("Liberty requires accountability.").

The lines of responsibility become blurred, and accountability for the exercise of power becomes less comprehensible, when Congress authorizes executive-branch employees to exercise duties of an "Officer of the United States" without subjecting their appointments to the strictures of the Appointments Clause. The growth of the Administrative State—with its ever-increasing oversight by individuals wielding significant power—demands accountability.

The decision below, if allowed to stand, would reduce that accountability. Petitioners here were

subjected to an administrative enforcement action initiated by the Enforcement Division of the Securities and Exchange Commission and conducted by an SEC Administrative Law Judge (ALJ). Pet. App. 37a-38a. In this proceeding, Administrative Law Judge Cameron Elliot heard testimony, including expert-witness testimony; accepted documents into evidence; considered and ruled on objections; weighed evidence; made factual findings; and reached legal conclusions. *Id.* at 115a-237a (ALJ Initial Decision on Remand). Judge Elliot ruled that Petitioners had violated the Investors Advisers Act of 1940, and issued sanctions: permanently barring Mr. Lucia from working as an investment advisor, revoking his (former) company's registration, and imposing civil penalties in the amount of $300,000. *Id.* at 235a.

Petitioners argued that this administrative proceeding was void on the ground that Judge Elliot was an "Officer of the United States" who had not been appointed under the Appointments Clause. Despite this Court's jurisprudence—instructing that an "Officer of the United States" is "'any appointee exercising significant authority pursuant to the laws of the United States,'" *Freytag*, 501 U.S. at 881 (quoting *Buckley v. Valeo*, 424 U.S. 1, 126 (1976))—a panel of the D.C. Circuit held that Judge Elliot was not an "Officer" within the meaning of the Appointments Clause. Pet. App. 9a-21a (disregarding *Freytag* and applying *Landry v. FDIC*, 204 F.3d 1125 (D.C. Cir. 2000)).

The Tenth Circuit reached the opposite conclusion. In *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016), the court held that an SEC administrative law judge was an "Officer" because, as in *Freytag*, (1) the

position was "established by law," (2) the duties, salary, and means of appointment were specified by statute, and (3) the ALJ "'exercise[d] significant discretion' in 'carrying out . . . important functions.'" *Id.* at 1179-82.

Therefore, this case presents the Court with a clear circuit split on a matter going to the heart of our constitutional structure: May Congress authorize administrative law judges from an executive-branch agency to conduct adjudicatory proceedings without providing for the proper appointments of those judges? That is, does the Constitution allow Congress to create offices in the Executive Branch without also requiring for the appointment of officers under the Appointments Clause?

Finally, as this Court has acknowledged that its "cases have not set forth an exclusive criterion for distinguishing between principal and inferior officers[,]" *Edmond*, 520 U.S. at 661, this case will allow the Court to clarify which Executive Branch employees are "Officers" and "inferior Officers" who must be appointed under the Appointments Clause.

For all of these reasons, this Court should grant the Petition.

ARGUMENT

I. THE CONSTITUTION ESTABLISHED A GOVERNMENT OF SEPARATED POWERS TO PROTECT INDIVIDUAL LIBERTY

"No political truth is certainly of greater intrinsic value, or is stamped with the authority of more enlightened patrons of liberty, than" this: "The accumulation of all powers, legislative, executive, and

judiciary, in the same hands, whether of one, a few, or many, and whether hereditary, self-appointed, or elective, may justly be pronounced the very definition of tyranny." *The Federalist No. 47*, at 324 (Madison) (J. Cooke ed. 1961).

To prevent tyranny, then, the Constitution divides the "powers of the . . . Federal Government into three defined categories, Legislative, Executive, and Judicial." *INS v. Chadha*, 462 U.S. 919, 951 (1983). Article I vests "[a]ll legislative Powers . . . in a Congress of the United States[;]" Article II vests "the" executive power "in a President of the United States of America[;]" and Article III vests "[t]he judicial Power of the United States . . . in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish." U.S. Const. art. I, § 1; art. II, § 1; art. III, § 1.

"The declared purpose of separating and dividing the powers of government, of course, was to 'diffus[e] power the better to secure liberty.'" *Bowsher v. Synar*, 478 U.S. 714, 721 (1986) (quoting *Youngstown Sheet & Tube Co. v. Sawyer*, 343 U.S. 579, 635 (1952) (Jackson, J., concurring)).

But the Framers knew that these mere "parchment barriers" between the branches were not a sufficient guarantor of liberty. *The Federalist No. 48*, at 333 (Madison) (J. Cooke ed. 1961). Therefore, the Constitution also "give[s] to each [branch] a constitutional control of the others," without which "the degree of separation which the maxim requires, as essential to a free government, [could] never in practice be duly maintained." *Id.* at 332. The "constant aim," Madison explained, was "to divide and arrange the several [branches] in such

a manner as that each may be a check on the other." *The Federalist No. 51*, at 349 (Madison) (J. Cooke ed. 1961).

In sum, so that individual liberty may be secured, the Constitution divides power into three branches but also gives to each branch certain powers to check the others. *See The Federalist No. 48*, at 332 (Madison) (J. Cooke ed. 1961):

> [P]ower is of an encroaching nature, and . . . it ought to be effectually restrained from passing the limits assigned to it. After discriminating, therefore, in theory, the several classes of power, as they may in their nature be legislative, executive, or judiciary, the next and most difficult task is to provide some practical security for each, against the invasion of the others.

See Metro. Wash. Airports Auth., 501 U.S. at 272 ("The structure of our Government as conceived by the Framers of our Constitution disperses the federal power among the three branches—the Legislative, the Executive, and the Judicial—placing both substantive and procedural limitations on each.").

In particular, "because 'the power of appointment to offices' was deemed 'the most insidious and powerful weapon of eighteenth century despotism[,]'" "manipulation of official appointments had long been one of the American revolutionary generation's greatest grievances against executive power." *Freytag*, 501 U.S. at 883 (quoting Gordon S. Wood, *The Creation of The American Republic 1776-1787*, 79, 143 (1969)).

Thus, the Appointments Clause—itself a microcosm of the Constitution's Separation of Powers.

II. WITHOUT STRICT ENFORCEMENT OF THE APPOINTMENTS CLAUSE, PUBLIC ACCOUNTABILITY AND INDIVIDUAL LIBERTY ARE THREATENED

A. The Appointments Clause Was Intended to Limit Executive and Legislative Power

The Appointments Clause "is among the significant structural safeguards of the constitutional scheme." *Edmond*, 520 U.S. at 659. It "embodies both separation of powers and checks and balances." *Bandimere*, 844 F.3d at 1172 (citation omitted). The Clause separates power by "defining unique roles for each branch in appointing officers." *Id.* And it ensures checks and balances by preventing appointments without the cooperation of the Executive and Legislative branches. The President may appoint principal officers only upon Senate approval. U.S. Const. art. II, § 2, cl. 2. "Inferior Officers" may be appointed, upon congressional authorization, only by the President alone, the Heads of Departments, or the Courts of Law. *Id.*

Of course, under the Necessary and Proper Clause, Congress may create "offices" and establish their duties. *See Buckley*, 424 U.S. at 38. But the Constitution "does not contemplate an active role for Congress in the supervision of officers charged with the execution of the laws it enacts." *Bowsher*, 478 U.S. at 722. Once Congress has "ma[de] its choice in enacting legislation, its participation ends. Congress can thereafter control the execution of its enactment

only indirectly—by passing new legislation." *Id.* at 733-34 (citing *Chadha*, 462 U.S. at 958). *See also Freytag*, 501 U.S. at 880 (The Appointments Clause "prevents Congress from dispensing power too freely; it limits the universe of eligible recipients of the power to appoint."); *Free Enterprise Fund v. Pub. Accounting Oversight Bd.*, 561 U.S. 477, 516 (2010) (Breyer, J., dissenting) (The separation-of-powers "principle, along with the instruction in Article II, § 3 that the President 'shall take Care that the Laws be faithfully executed,' limits Congress' power to structure the Federal Government.").

But here, Congress has avoided the strictures of the Appointments Clause by granting to the agents of administrative agencies vast authority without designating those employees as "Officers" within the meaning of the Appointments Clause.[2] In this way, Congress has "'mask[ed], under complicated and indirect measures, the encroachments which it makes on the co-ordinate departments,' [The Federalist], No. 48, p. 310 [(C. Rossiter ed. 1961)] (J. Madison), and thus control[s] the nominal actions (*e.g.*, appointments) of the other branches." *Freytag*, 501 U.S. at 906 (Scalia, J., concurring in part and concurring in the judgment) (citing Thomas Jefferson, *Notes on the State of Virginia* 120 (William Peden ed. 1955)).

And by thus removing from the President (or department heads or courts of law) the power to appoint officers, Congress has arrogated to itself

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[2] As Petitioners note, Congress does refer to the SEC's administrative law judges as "officers." *See* Pet. 3-4. But Congress does not require that these "officers" be appointed under the Appointments Clause.

significant Executive power—a danger the Framers sought to prevent. *See Chadha*, 462 U.S. at 947 (explaining that the Framers recognized the particular "'propensity'" of the legislative branch "'to invade the rights of the Executive'") (quoting *The Federalist No. 73*, at 494 (Hamilton) (J. Cooke ed. 1961).

B. The Appointments Clause Was Also Intended To Limit the Diffusion of the Appointment Power to Protect the Governed and Increase Accountability

The limits set forth in the Appointments Clause do not exist simply to settle inter-branch squabbles over control of the government. Rather, these limitations go to the heart of a self-governing people. As the Framers understood, "by limiting the appointment power, they could ensure that those who wielded it were accountable to political force and the will of the people." *Freytag*, 501 U.S. at 884. And the appointment of "Officers" under the Appointments Clause was one means of holding the President accountable: the President is "directly dependent on the people, and since there is only *one* President, *he* is responsible. The people know whom to blame." *Morrison v. Olson*, 487 U.S. 654, 729 (1988) (Scalia, J., dissenting) (emphasis in the original).

Whom should Mr. Lucia blame? He and his (former) company were subjected to a proceeding affecting his fundamental right to pursue an avocation. *See Cummings v. Missouri*, 71 U.S. 277, 321-22 (1866). This proceeding, however, was initiated by agents of the SEC and overseen by another agent of the SEC. And the ALJ who presided over this proceeding wielded significant authority—

permanently barring Mr. Lucia from working as an investment adviser—despite not having been appointed under the Appointments Clause. Is Congress to blame for establishing this administrative process? Or is the President accountable for administering the laws against Petitioners? Mr. Lucia, and others facing the ever-growing Administrative State, should not have to guess whom to hold accountable. *See Ass'n of Am. R.R.s*, 135 S. Ct. at 1234 (Alito, J., concurring) ("Liberty requires accountability."). *See also Free Enterprise Fund*, 561 U.S. at 499 ("Our Constitution was adopted to enable the people to govern themselves, through their elected leaders. The growth of the Executive Branch, which now wields vast power and touches almost every aspect of daily life, heightens the concern that it may slip from the Executive's control, and thus from that of the people.").[3]

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[3] A common justification for the modern administrative state is efficiency or convenience. *See* Pet. App. 4a-5a (*Lucia* opinion) (discussing Congress' authorizing the SEC to delegate certain functions for greater flexibility and efficiency). This Court has repeatedly rejected the argument that efficiency trumps the Constitution's limitations. *See, e.g.*, *Chadha*, 462 U.S. at 959 (explaining that there is "no support in the Constitution or decisions of this Court for the proposition that the cumbersomeness and delays often encountered in complying with explicit Constitutional standards may be avoided, either by the Congress or by the President.").

The Appointments Clause itself recognizes the need for convenience in certain circumstances: The "obvious purpose" in authorizing Congress to vest appointment power of "inferior Officers" in the President alone, in the Courts of Law, or in the Heads of Departments, is "administrative convenience." *Edmond*, 520 U.S. at 660 (citing *United States v. Germaine*, 99 U.S. 508, 510 (1879)). But the Constitution permits no further

Indeed, precisely because bureaucracy is the "ultimate black box of government—the place where exercises of coercive power are most unfathomable and thus most threatening . . . [T]he need for transparency, as an aid to holding governmental decisionmakers to account, here reaches its apex." Kagan, *supra*, at 2332.

This Court should grant Mr. Lucia's Petition and reinforce the doctrine of Separation of Powers, which was established to protect the people's liberties.

III. THIS COURT'S GUIDANCE IS NEEDED

Finally, the important nature of the issues before the Court is matched by the need for clarity. This Court has stated that an "Officer of the United States" is "'any appointee exercising significant authority pursuant to the laws of the United States,'" who "'must, therefore, be appointed in the manner prescribed by'" the Appointments Clause. *Freytag*, 501 U.S. at 881 (quoting *Buckley*, 424 U.S. at 126). In *Freytag*, this Court concluded that the office of "special trial judge" within the U.S. Tax Court had been "established by Law" (the "duties, salary, and means of appointment for that office are specified by statute"); and that these special trial judges exercise significant discretion in carrying out their "important functions" (taking testimony, conducting trials, ruling on admissibility of evidence, and having power to enforce compliance with discovery orders). *Freytag*, 501 U.S. at 881-82. And because of these "significant authorities," the judges' inability to enter final

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"convenience." Congress may not allow, as here, the "appointment" of inferior officers like ALJs outside of the Appointments Clause.

decisions was not, contrary to the government's arguments, dispositive. *Id.* Therefore, special trial judges are "inferior Officers" within the meaning of the Appointments Clause.

But this "significant authority" prong has led lower courts to different analyses and conclusions—as the circuit split here shows.

The *Bandimere* opinion applied a test derived from *Freytag*. *Id.*, 844 F.3d at 1174-76. *Bandimere* concluded that an SEC administrative law judge was an "Officer" because, as in *Freytag*, (1) the position was "established by law," (2) the duties, salary, and means of appointment were specified by statute, and (3) the ALJ "'exercise[d] significant discretion' in 'carrying out . . . important functions.'" *Bandimere*, 844 F.3d at 1179-82.

The D.C. Circuit, however, applied its decision in *Landry*, 204 F.3d 1125, rather than this Court's *Freytag* opinion. *See* Pet. App. 13a ("[T]o the extent petitioners contend that the approach required by *Landry* is inconsistent with *Freytag* or other Supreme Court precedent, this court has rejected that argument and *Landry* is the law of the circuit[.]") (citation omitted). According to the *Lucia* panel, once an individual "meets the threshold requirement that the relevant position was established by Law and the position's duties, salary, and means of appointment are specified by statute[,]" the "main" criteria for distinguishing inferior Officers from employees (who are not covered by the Appointments Clause) are: "(1) the significance of the matters resolved by the officials, (2) the discretion they exercise in reaching their decisions, and (3) the finality of those decisions." *Id.* 12a (internal quotation marks and citations

omitted). The panel's decision, however, turned on its conclusion that an SEC administrative law judge cannot enter a final decision. *Id.* 13a-16a. As noted, this factor is not dispositive. *Freytag*, 501 U.S. at 881-82.

Regardless, this Court also recognizes that its "cases have not set forth an exclusive criterion for distinguishing between principal and inferior officers." *Edmond*, 520 U.S. at 661. And while *Freytag* may present the best analysis for deciding whether SEC administrative law judges are "Officers," a definitive test would allow lower courts to address an issue whose importance grows along with the size and scope of the Administrative State.

Importantly, it is not clear as a matter of original meaning or as a matter of this Court's jurisprudence that the authority exercised by an employee need be "significant" for that employee to be an "Officer." *See* Jennifer L. Mascott, *Who Are "Officers of the United States?"*, 70 Stan. L. Rev. --- (forthcoming 2018) (demonstrating that the original public meaning of "officer" is "anyone with ongoing responsibility for a statutory duty").[4] The *Bandimere* court identified numerous positions previously held to be "Officers" by this Court:

> • a district court clerk, *In re Hennen*, 38 U.S. (13 Pet.) 230, 258 (1839);
>
> • an "assistant-surgeon," *United States v. Moore*, 95 U.S. 760, 762 (1877); [and]

[4] The latest draft of this article may be found here: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2918952.

- "thousands of clerks in the Departments of the Treasury, Interior, and the othe[r]" departments, *Germaine*, 99 U.S. at 511.

Bandimere, 844 F.3d at 1173-74; *see id.* at 1174 (collecting additional examples).

Here, Congress not only refers to SEC ALJs as "officers of the Commission," 15 U.S.C. §§ 77u, 78v, 80a-40, 80b-12; but Congress has also established their duties and salary by law, 5 U.S.C. §§ 556-557 (duties), 5372(b) (salary). And while the SEC's ALJs certainly execute "significant authority" to meet this Court's test in *Freytag* (*see* Pet. 14-16) (listing the SEC ALJs' various powers),[5] they also qualify as "Officers of the United States" under the original meaning and this Court's jurisprudence.

The Court should grant the Petition and adopt a test for identifying "Officers of the United States" that is based on the original meaning of the Appointments Clause and this Court's earlier jurisprudence.

CONCLUSION

The "purpose of the separation and equilibration of powers in general, and of the unitary Executive in particular, was not merely to assure effective government but to preserve individual freedom."

[5] The importance of the functions carried out by the SEC's administrative law judges is demonstrated by the SEC's position that ALJs are "independent." *See, e.g.*, *Bandimere*, 844 F.3d at 1176-77 and n.11. Thus, by the SEC's own lights, its ALJs are not "mere" employees.

Morrison, 487 U.S. at 654 (Scalia, J., dissenting). And the "hydraulic pressure inherent within each of the separate Branches to exceed the outer limits of its power, even to accomplish desirable objectives, must be resisted." *Chadha*, 462 U.S. at 951. While each branch's interpretation of its own powers is entitled to "great respect," in the end, "'[i]t is emphatically the province and duty of the judicial department to say what the law is.'" *United States v. Nixon*, 418 U.S. 683, 703 (1974) (quoting *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 177 (1803)).

This Court should grant the Petition and reinvigorate the Constitution's fundamental protections of liberty guaranteed by its carefully structured separation of powers.

DATED: August 2017.

Respectfully submitted,

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RAYMOND J. LUCIA, *ET AL.*,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

AMICUS CURIAE BRIEF OF ANTHONY MICHAEL SABINO IN SUPPORT OF RESPONDENT

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INTEREST OF *AMICUS CURIAE*

This *amicus curiae* is a law professor with expertise in constitutional law, securities regulation, and securities litigation. Furthermore, this *amicus curiae* has represented parties in proceedings before the Securities and Exchange Commission (the "SEC" or the "Commission"), and regularly lectures on the precise topics found in the instant Petition. This case implicates, *inter alia*, the Appointments Clause of Article II of the Constitution, judicial review of administrative agency action, and the proper conduct of enforcement proceedings before the SEC. This *amicus curiae* has a professional and scholarly interest in the proper application and development of the law in these domains.[1]

STATEMENT

This *amicus curiae* respectfully adopts, in relevant part, the Statement of Facts set forth in the Petition for Certiorari filed by the Petitioners herein, Raymond J. Lucia, *et al.* (hereinafter, "Petitioners").

[1] No counsel for a party authored this brief in whole or in part, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. Counsel of record received timely notice of the intent to file this brief, as required by Supreme Court Rule 37.2(a). Petitioners and Respondent consented to this filing.

SUMMARY OF ARGUMENT

Denying review herein shall avoid an Appointments Clause question pertaining to the present mode of appointing SEC Administrative Law Judges ("ALJs"), avoid systemic risk to ALJs now adjudicating matters at a wide range of administrative agencies, propagate the appropriate judicial restraint heretofore exercised by a significant number of circuit courts which have avoided the constitutional question herein by resolving substantially similar controversies upon jurisdictional grounds, recognize that these same tribunals have yet to address said constitutional question, and avoid needlessly revisiting existing precedent regulating the proper functioning of the Appointments Clause.

ARGUMENT

I. DENYING REVIEW WILL AVOID BOTH THE CONSTITUTIONAL QUESTION AND THE SYSTEMIC RISK FOR ALJs ACROSS A WIDE RANGE OF ADMINISTRATIVE BODIES.

It is axiomatic that the courts should avoid resolving constitutional questions whenever possible. "If there is one doctrine more deeply rooted than any other in the process of constitutional adjudication, it is that [the Court] ought not to pass on questions of constitutionality . . . unless such adjudication is unavoidable." *Zobrest v. Catalina Foothills School District*, 509 U.S. 1, 14 (1993) (Blackmun, J., dissenting) (quotation

and citation omitted). This "fundamental rule of judicial restraint" enjoys the sanction of "time and experience." *Id.* (Blackmun, J., dissenting) (quotation and citation omitted). It serves an essential need to protect both "the law and the adjudicatory process." *Id.* at 16 (Blackmun, J., dissenting).

That "fundamental rule of judicial restraint" has been respected in full by a significant number of the appellate courts adjudicating matters substantially similar to the case at bar. In those controversies, as in the instant case, the authority of SEC ALJs to hold office and preside over Commission enforcement proceedings was called into question. Choosing to resolve the cases before them upon jurisdictional grounds, the relevant tribunals wisely avoided a potential constitutional quagmire. *See* Point II, *infra*. While not yet constituting a strict numerical majority of all the circuits, these panel decisions evince a consensus of reasoning eminently rational and reasonable in light of the constitutional precept noted above.

Furthermore, these circuit courts were not merely being adroit. Each of these panels was faithful to the overarching imperative of avoiding a constitutional question wherever possible. Denying review here would not only appropriately resolve the case at bar, it would bestow an imprimatur upon the circumspection exercised by the relevant tribunals which have confronted substantially similar controversies. *Id.*

In sum, the courts do not decide constitutional questions "needlessly." *Zobrest*, *supra*, 509 U.S. at 16 (Blackmun, J., dissenting). Denying review of the case at bar shall properly honor that precept of judicial restraint.

An additional point merits attention at this juncture. SEC ALJs oversee proceedings pertaining to the enforcement of the federal securities acts. For some eight decades, those statutory regimes have assured disclosure, transparency, and honesty in our vital capital markets. *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 170-71 (1994). The Commission's administrative adjudicators play a key role in accomplishing those objectives. Judicial restraint should therefore be exercised before upending their authority within that regulatory scheme.

The immediately preceding observation regarding SEC ALJs is highly relevant to a more global concern. If review of the case at bar is granted, SEC ALJs would not be the only denizens of the administrative state that would be put in harm's way.

Consideration of the constitutional question advanced herein will undoubtedly have repercussions for *all* ALJs at *all* administrative agencies. This is no small matter, as the following amply demonstrates.

There are reportedly a total of 1,792 administrative law judges in service to federal agencies today, and 1,537 Social Security Administration ALJs alone "collectively handle hundreds of thousands of hearings a year." *Bandimere v. SEC*, 844 F.3d 1168, 1199 and 1199

n.5 and n. 6 (10th Cir. 2016) (McKay, J., dissenting) (citations omitted). Such facts are already well known to the Court. *See Free Enterprise Fund v. Public Company Accounting Oversight Board*, 561 U.S. 477, 586 app. C (2010) (Breyer, J., dissenting) (noting in excess of 1,500 ALJs in the employ of the federal government at that time). It is common knowledge that these agencies and their in-house adjudicators act upon matters of grave importance to ordinary Americans and the latter's everyday lives. *See Bandimere*, *supra*, 844 F.3d at 1201 (McKay, J., dissenting).

Granting review herein brings the potential for chaos. It might very well unleash an untold number of challenges against ALJs across a broad spectrum of agencies, and endanger the everyday administrative adjudications alluded to above. If review of the case at bar is granted, "all federal ALJs are at risk," with the further possibility of "effectively render[ing] invalid thousands of administrative actions." *Bandimere*, *supra*, 844 F.3d at 1199 (McKay, J., dissenting). Such systemic risk cannot be justified in the present circumstances.

In sharp contrast, denying review here would avoid such perils. As point in fact, the significant circuit consensus which has declined to address the constitutional question, *see* Point II, *infra*, has effectively preserved the *status quo* for SEC ALJs specifically and administrative law judges in general. Propagating such judicial restraint will avoid not only the constitutional question, but the potential for harm on a much vaster scale than the case at bar contemplates.

In sum, granting review of the instant case would not only impact SEC ALJs and the agency they toil for, but imperil nearly 2,000 adjudicators at a diversity of administrative agencies. Avoiding the *gravitas* of the constitutional question presented here shall avoid that systemic risk. Accordingly, review should be denied.

For all the foregoing reasons, it is respectfully suggested that review not be granted.

II. DENYING REVIEW IS APPROPRIATE GIVEN THAT THE MAJORITY OF CIRCUITS TO HAVE ADDRESSED SIMILAR CONTROVERSIES HAVE LIMITED THEIR RULINGS TO JURISDICTIONAL GROUNDS, AND HAVE YET TO OPINE UPON THE CONSTITUTIONAL QUESTION PRESENTED.

It is imperative that the history of the contemporary controversy surrounding the authority of SEC ALJs be considered before deciding whether review should be granted in the case at bar. Certainly, it is beyond peradventure that the circuit court decision below is contradicted by a holding of one of its appellate brethren. Yet there is a deal more to be said concerning the state of relevant appeals court rulings regarding the matter at hand, a great deal more indeed. Therefore, the evolution of the existing conflict must be described in some detail.

In the wake of the Great Recession, remedial legislation "dramatically expanded" the authority of the

SEC to bring enforcement actions before its in-house ALJs. *Tilton v. SEC*, 824 F.3d 276, 278-79 (2d Cir. 2016), *cert. denied*, ___ U.S. ___, 137 S. Ct. 29 (2016). Respondents were thus provoked to vigorously contest the power of the Commission's adjudicators to preside over such controversies. *Id.* at 279. Now acting as plaintiffs, these objects of SEC enforcement cases nearly always invoked the holding of *Free Enterprise Fund*, *supra*, 561 U.S. at 484 and 492, in support of the argument that, identical to the accounting industry oversight board members at the center of that landmark, SEC ALJs likewise hold office in violation of the Appointments Clause of Article II. U.S. Const. Art. II, § 2, cl. 2.

The instant controversy's first iteration resulted in a significant number of conflicting district court decisions, espousing a multitude of disparate approaches to the question. Pertinent to the case at bar, a number of trial judges prioritized the Appointments Clause question. *See generally* Michael A. Sabino & Anthony Michael Sabino, "Challenging the Power of SEC ALJs: A Constitutional Crisis or a More Nuanced Approach?" 43 *Securities Regulation Law Journal* 369 (2015) (analyzing the then-extant cases) (hereinafter "*Challenging SEC ALJs*").

Notwithstanding the initial dissonance, contentiousness between the courts below eventually dissipated, for the most part. As these contests percolated to the appellate level, a significant number of the circuits quickly coalesced around a shared rationale. At the center of their respective analyses was *Thunder*

Basin Coal Co. v. Reich, 501 U.S. 200 (1994), with its express delineation of only the most narrow of opportunities for asserting jurisdiction over administrative agency action, and its concomitant disfavoring of liberal judicial intercession in such proceedings. *See Challenging SEC ALJs*, *supra*, at 372 and 380 (synthesizing the sophisticated *Thunder Basin* analytical triad and its progeny).

Thus, a degree of harmony was restored as a significant number of appellate panels applied the three-pronged test of *Thunder Basin*, and denied relief on the basis of the jurisdictional maxims articulated therein. Moreover, in so constraining their mode of analysis, these tribunals successfully avoided the Appointments Clause question altogether. *Bebo v. SEC*, 799 F.3d 765, 767-68 (7th Cir. 2015), *cert. denied*, ___ U.S. ___, 136 S. Ct. 1500 (2016); *Jarkesy v. SEC*, 803 F.3d 9, 29-30 (D.C. Cir. 2015); *Tilton*, *supra*, 824 F.3d at 279 and 291; *Hill v. SEC*, 825 F.3d 1236, 1237 and 1241 (11th Cir. 2016); *and Bennett v. SEC*, 844 F.3d 174 (4th Cir. 2016).

To be sure, each circuit court inscribed its own nuances upon the teachings of *Thunder Basin*. *See Tilton*, *supra*, 824 F.3d at 279 and 282 (apparently giving equal weight to all three jurisdictional factors, and further emphasizing the "closer questions" presented therein on the last two legs of the *Thunder Basin* test); *Hill*, *supra*, 825 F.3d at 1250 (finding the last two requirements of *Thunder Basin* "do not cut strongly either way and thus do not persuade us"); *Bennett*, *supra*, 844 F.3d at 183 and 183 n.7 (while seeming to consider

all three elements of *Thunder Basin*, nevertheless declaring in a parenthetical the first prong of *Thunder Basin* is "the most important"); *Jarkesy*, *supra*, 803 F.3d at 22 (*Thunder Basin* provides "guideposts for a holistic analysis"); *compare Bebo*, *supra*, 799 F.3d at 773 (stressing the importance of *Elgin v. Dep't of Treasury*, 567 U.S. 1 (2012), to its jurisdictional analysis). In this manner, nearly half of the courts of appeals gave a wide berth to the constitutional question posed here.

Four salient points emerge from the foregoing.

First, these circuit courts never reached the constitutional question posed in the instant case. Accordingly, we lack the benefit of their present thinking upon that important issue.

Furthermore, without relevant pronouncements from this significant number of appellate courts, we cannot confirm if there truly is an intercircuit conflict in need of resolution. This provides an additional reason for abstaining from review of the question presented, at least until some or all of the tribunals cataloged above promulgate more lucid expressions of their perspectives upon the pending controversy.

Second, each of these august tribunals wisely selected a path far less likely to instigate a constitutional cataclysm. By confining their reasoning to jurisdictional grounds alone, each engaged in a commendable exercise of judicial restraint. This discretion by the courts below strongly favors extending that same circumspection to the case at bar.

Third, the circuit decisions examined hereinabove demonstrate a remarkable cohesiveness amongst themselves. Notwithstanding their individual gloss upon landmarks such as *Thunder Basin*, these panel opinions are strikingly consistent in their respective modes of reasoning, insofar as they are delimited to jurisdictional predicates. This also cuts against the notion that there exists an irredeemable circuit conflict that can only be reconciled by granting review of the instant case.

Fourth, while the tribunals enumerated above have forged a consensus (albeit a rough one), this subgroup nonetheless represents, numerically, less than half of the total number of circuit courts. This fact stands in counterpoise to the securities law proviso which guarantees that any person aggrieved by a decision of the SEC may seek review before the circuit court of appeals where she resides or does business. 15 U.S.C. § 78(y)(1). *See, i.e., Bennett, supra*, 844 F.3d at 177.

It cannot be denied that the statute contemplates, indeed outright invites, a nationwide response from *all* of the appellate courts upon matters such as the question presented here. The geographic dispersion of the circuit decisions noted above testifies, at least in part, to the truth that this statutory prerogative leaves wide open the possibility (one might even say the probability) that additional tribunals shall come to opine on some or all of the same issues found in the case at bar. Put another way, it can be said that the instant controversy is still in a nascent stage, and requires further

growth before being classified as a genuine internecine conflict, divisive enough to merit review.

Certainly, it is beyond argument that there is an irreconcilable conflict between *Bandimere* and the case at bar. *Bandimere*, *supra*, 844 F.3d at 1182 (expressly disagreeing with the holding below in the instant case). *See also* Petition for Certiorari at 19. But can review be justified when the discord is thus far cabined to only two tribunals?

More to the point, that pair of diametrically opposed appellate decisions must be carefully weighted in counterpoise to the larger subset of circuit court rulings set forth above, each one of the latter confined to jurisdictional grounds, and without reference to the constitutional question proffered in the instant case. It is once more respectfully suggested that a true internecine circuit conflict necessitating review presupposes a conflagration far more severe that the one evident here.

In sum, with the constitutional question in the case at bar not yet addressed in the present circumstances by a clear majority of the circuits, with a significant number of tribunals having exercised judicial restraint, to wit, avoiding said question and instead coalescing upon jurisdictional grounds for their *ratio decendi*, with an irrefutable statutory opportunity for more appellate courts to be heard on the question at hand, and with but two circuits in polar opposition regarding these matters, the aggregation of these factors does not favor review.

For these reasons, it is respectfully suggested that review not be granted.

III. THE LOWER COURTS HAVE DISTINGUISHED *FREE ENTERPRISE FUND* FROM THE CONTROVERSY AT HAND, AND THEREFORE REVIEW NEED NOT BE GRANTED ON THAT ACCOUNT.

To preserve our ordered system of liberty from the excesses of executive power, the Framers acted upon a fundamental and inarguable precept. "Liberty requires accountability." *Dep't of Transportation v. Association of American Railroads*, 575 U.S. ___, ___, 135 S. Ct. 1225, 1234 (2015) (Alito, J., concurring). In recognition of that basic truth, the Framers incorporated several "accountability checkpoints" into the Constitution, *id.*, 575 U.S. at ___, 135 S. Ct. at 1237 (Alito, J., concurring), each one securing separation of powers and checks and balances.

Prominent among them is the Appointments Clause, a "structural safeguard" that tethers federal officers to the "sovereign power of the United States, and thus to the people." *Bandimere, supra*, 844 F.3d at 1188 (Briscoe, J., concurring). Above all else, the Appointments Clause insists that those who wield executive authority remain "accountable to political force and the will of the people." *Freytag v. Commissioner of Internal Revenue*, 501 U.S. 868, 884 (1991).

For nearly a decade, *Free Enterprise Fund, supra*, has been the pivot upon which Appointments Clause

controversies have turned. *See, i.e., PHH Corp. v. Consumer Financial Protection Bureau*, 839 F.3d 1, 7 (D.C. Cir. 2016), *rehearing* ***en banc*** *granted, order vacated*, ___ F.3d ___ (February 16, 2017) (oral argument for the *en banc* hearing held May 27, 2017). Notwithstanding the eminence of *Free Enterprise Fund* as a guardian of separation of powers and checks and balances, it need not, in truth, be applied to every single instance where the authority of an administrative agency adjudicator is called into question.

At least two of the relevant circuit court decisions set forth hereinabove held that the controversies before them regarding the authority of SEC ALJs were distinguishable on their facts from *Free Enterprise Fund*. *See, i.e., Hill, supra*, 825 F.3d at 1247-48 (the complainant was "not in the type of precarious position the Supreme Court found unacceptable in *Free Enterprise Fund*"); *Bennett, supra*, 844 F.3d at 182 and 186 (distinguishing on the facts, and declaring the plaintiff "reads too much into" and further "misreads" *Free Enterprise Fund*).

Thus, there is no misapprehension of *Free Enterprise Fund* in need of correction here. Quite to the contrary, the abovementioned circuit decisions ably demonstrate that the lower courts are fully capable of either applying or distinguishing *Free Enterprise Fund* on factual grounds, as circumstances necessitate.

Respectfully, review need not be granted on that account.

This *amicus* respectfully suggests that any of the three points hereinabove would constitute sufficient cause to deny review. The presence of all three suggests even more strongly that review should be denied.

CONCLUSION

Respectfully, for all the reasons set forth above, the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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September 2017

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No. 17-130

IN THE
Supreme Court of the United States

RAYMOND J. LUCIA
AND RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ Of Certiorari
To The United States Court Of Appeals
For The District Of Columbia Circuit

BRIEF FOR PETITIONERS

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

All parties to the proceeding are named in the caption.

Pursuant to this Court's Rule 29.6, undersigned counsel state that petitioner Raymond J. Lucia Companies, Inc. has no parent corporation, and no publicly held company holds 10% or more of its stock.

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BRIEF FOR PETITIONERS

Petitioners Raymond J. Lucia and Raymond J. Lucia Companies, Inc. (collectively, "Lucia") respectfully submit that the judgment below should be reversed.

OPINIONS BELOW

The *per curiam* order of the en banc court of appeals, Pet. App. 1a-2a, is available at 868 F.3d 1021. The panel's opinion, Pet. App. 3a-36a, is reported at 832 F.3d 277. The opinion and order of the Commission, Pet. App. 37a-109a, are available at Exchange Act Release No. 73,857, 2015 WL 5172953; an interim remand order, Pet. App. 238a-243a, is unreported. The relevant initial decision of the administrative law judge, Pet. App. 115a-237a, is available at Initial Decision Release No. 495, 2013 WL 3379719.

JURISDICTION

The judgment of the court of appeals was entered on June 26, 2017. Pet. App. 1a. The petition for a writ of certiorari was filed on July 21, 2017 and was granted on January 12, 2018. This Court has jurisdiction under 28 U.S.C. § 1254(1).

CONSTITUTIONAL, STATUTORY, AND REGULATORY PROVISIONS INVOLVED

The Appointments Clause as well as pertinent statutory and regulatory provisions are reproduced in the Petition Appendix at 247a-294a.

STATEMENT

Administrative law judges of the Securities and Exchange Commission preside over trial-like adversarial hearings, during which they take testimony, rule on the admissibility of evidence, and enforce compliance with their orders. This Court has ruled that federal adjudicators who exercise substantially similar powers are "'Officers of the United States'" within the meaning of the Appointments Clause. *Freytag* v. *Comm'r*, 501 U.S. 868, 881-82 (1991); *see also Edmond* v. *United States*, 520 U.S. 651, 662, 665 (1997). The question presented is whether SEC ALJs are also Officers.

1. Long before the advent of the modern administrative state, the Framers understood that curbing abuses of executive power requires carefully cabining the prerogative to *appoint* those who wield it. *Edmond*, 520 U.S. at 659-60. In prescribing the means of appointing any "Office[r] of the United States," U.S. Const. art. II, § 2, cl. 2, the Appointments Clause "preserves ... the Constitution's structural integrity" by ensuring that officials who make and receive appointments remain, directly or indirectly, "accountable to political force and the will of the people." *Freytag*, 501 U.S. at 878, 884; *see also Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam).

a. Congress has charged the SEC with executing and enforcing the federal securities laws, 15 U.S.C. § 78d(a), including the Investment Advisers Act of 1940, *id.* § 80b-9. Congress authorized the Commission to "delegate ... any of its functions," except rulemaking, to "administrative law judge[s]." *Id.* § 78d-1(a). When the Commission initiates an enforcement action, it can either sue in federal court or commence an administrative proceeding. *See id.* §§ 78u, 78u-2,

78v. Where the Commission elects the latter course, an ALJ normally presides over the proceeding. *See* 17 C.F.R. § 201.110.

In authorizing ALJs to resolve contested matters "on the record" pursuant to the Administrative Procedure Act, 5 U.S.C. § 557(c)(3)(A), "Congress intended to make [such officials] 'a special class of semi-independent'" yet still "'subordinate hearing officers,'" *Ramspeck* v. *Fed. Trial Exam'rs Conference*, 345 U.S. 128, 132 (1953) (citation omitted). Congress repeatedly referred to SEC ALJs as "officers" in the securities laws, 15 U.S.C. §§ 77u, 78v, 80a-40, 80b-12, and to their precursors as "officers" or "subordinate officers" in the APA, Pub. L. No. 79-404, 60 Stat. 237, 241-42 (1946). Congress also set forth SEC ALJs' duties and salary by law, *see* 5 U.S.C. §§ 556-57 (duties), 5372(b) (salary); and prescribed that the "*agency* shall appoint [its] administrative law judges," *id.* § 3105 (emphasis added)—an obligation the Commission has failed to discharge. ALJs are removable "for good cause, as established and determined by the Merit Systems Protection Board." *Id.* § 7521(a).

b. Since the Dodd-Frank Act of 2010 expanded the Commission's administrative enforcement authority, the Commission has brought more than 80% of its enforcement proceedings in its in-house tribunal, where it has won over 90% of the time. *See* Jean Eaglesham, *SEC Wins With In-House Judges*, Wall St. J. (May 6, 2015), http://tinyurl.com/o9vsozr (all Internet sites last visited February 20, 2018).

The Commission has characterized its ALJs as "hearing officer[s]" and delegated to those "officer[s] ... the authority to do all things necessary and appropriate to discharge" their duties. 17 C.F.R. § 201.111. That authority is extensive and includes the powers

to oversee hearings and discovery, rule on motions (including for summary disposition), enter default judgments, and impose or modify sanctions. *See generally ibid.* (non-exhaustive list of ALJs' powers); *see also id.* §§ 201.155 (default), .180 (sanctions), .230 (document production), .232-.234 (subpoenas and depositions), .250 (summary disposition), .320-.326 (evidence). As the Commission emphasized in this proceeding, ALJs play a "vital role" in the agency's decision-making process, Pet. App. 241a, by ruling on the admissibility of evidence, taking testimony, and making credibility findings.

At the conclusion of an administrative hearing, SEC ALJs enter an "initial decision," 17 C.F.R. § 201.360(a)(1), that can and almost always does "become final" without any Commission review, *id.* § 201.360(d)(2). Although the Commission "retain[s] a discretionary right to review" any "action" by an ALJ, whether *sua sponte* or upon a petition for review, 15 U.S.C. § 78d-1(b), "[i]f the right to exercise such review is declined" or is not timely sought, the ALJ's action is "deemed the action of the Commission," *id.* § 78d-1(c); 17 C.F.R. § 201.360(d)(2).

SEC ALJs are not appointed in a manner that complies with the Appointments Clause. Pet. App. 9a-10a. Although the Commission acting as a body is considered a "Head of Department" under the Clause, *Free Enter. Fund* v. *PCAOB*, 561 U.S. 477, 512-13 (2010), the Commission itself does not appoint its ALJs. Rather, SEC ALJs are selected by SEC staff from a list of three candidates provided by the Office of Personnel Management. Pet. App. 295a-297a.

2. Petitioner Raymond J. Lucia, formerly the sole owner of petitioner Raymond J. Lucia Companies, Inc., is an investment professional who—until this

proceeding—had an unblemished record spanning nearly forty years. *See* Pet. App. 34a, 119a-120a, 233a. In free seminars for potential clients, Lucia promoted a retirement strategy colorfully named "Buckets of Money" ("BOM"), which advocated a diversified portfolio from which, in retirement, investors would liquidate lower-risk investments first to give riskier investments time to grow. *Id.* 23a, 127a-129a.

Lucia used a slideshow that compared fictional investors following his BOM strategy with investors following other strategies in hypothetical scenarios. Pet. App. 23a, 130a-132a. Two hypotheticals, which the slides described as "backtests," were based partly on historical periods—using actual data for certain stock returns, but employing assumptions regarding inflation and rates of return on real-estate and other investments. *Id.* 46a-47a.

Lucia stressed that these examples were hypothetical. Slides illustrating the examples were emblazoned: "This is a hypothetical illustration and is not representative of an actual investment." Pet. App. 43a n.10. And slides outlining the BOM strategy noted that "[r]ates of return are hypothetical in nature and are for illustrative purposes only." *Id.* 45a n.14, 47a n.19. Mr. Lucia "'expressly informed seminar attendees that he was using *hypothetical, pretend, assumed* rates of return.'" *Id.* 76a; *see, e.g.*, *id.* 47a-48a.

Before Lucia's slideshow was publicly distributed, it was reviewed by broker-dealers registered with the Financial Industry Regulatory Authority, who repeatedly approved the slides and raised no concerns that they were misleading. Pet. App. 84a; *see* FINRA R. 3110 ("Supervision"). In 2003, the Commission's examination staff reviewed a similar version of Lucia's

slideshow and raised no concerns that it was misleading. Pet. App. 84a.

No securities were offered or sold at Lucia's seminars. Pet. App. 39a n.2, 82a. Instead, seminar attendees interested in a "complimentary financial planning consultation" could complete a response card requesting to be contacted. *Id.* 41a n.6. About 50,000 people attended Lucia's seminars over the years, but not one lodged a complaint that the slideshow was misleading. *Id.* 129a, 206a.

3. In 2012, the Commission charged Lucia with violating the antifraud provisions of the Investment Advisers Act and SEC rules. Pet. App. 7a-8a. The allegations focused on two presentation slides—out of a 126-page slideshow, *id.* 130a—that used the word "backtest" to describe the hypothetical comparisons. *Id.* 66a. Although the term "backtest" was not defined in any law or regulation, and had not been construed in any judicial or administrative proceeding, the Enforcement Division insisted that a "backtest" must be based *exclusively* on historical data, and that Lucia's use of the term "backtest" to describe hypotheticals that used assumptions was therefore misleading even though the assumptions themselves were disclosed. C.A.D.C. JA30.

The Commission could have sued Lucia in federal court, *see* 15 U.S.C. § 78d-1, but it chose not to. Instead, the Commission assigned the proceeding to ALJ Cameron Elliot, who would not rule against the Enforcement Division once in his first fifty cases (including this one). *See* Sarah N. Lynch, *SEC Judge Who Took on the "Big Four" Known for Bold Moves*, Reuters (Feb. 3, 2014), http://tinyurl.com/hlu76fl. After Judge Elliot issued an initial decision, the Commission remanded for further factual findings, Pet.

App. 239a, because such findings were "a matter of considerable importance" to the Commission, *id.* 241a.

Judge Elliot shaped the record by crediting the testimony of two seminar audience members, *see* Pet. App. 160a-161a, 193a, which was essential to his findings that Lucia had made materially false statements, *see id.* 169a, 190a, 191a, 211a. One of these witnesses had previously sued Lucia, but then "admitted in writing that his claims against Lucia were false." *Id.* 193a. Judge Elliot credited this person's testimony, even while excluding evidence showing that he had made "knowingly false sworn statements." *Ibid.* The other witness had "holes in his memory" and had "complained to multiple people" about Lucia (though not about the BOM seminar), but Judge Elliot found that this only "bolster[ed] his overall credibility." *Id.* 194a. Meanwhile, Judge Elliot did not mention that other witnesses would have testified on behalf of Lucia, but the Enforcement Division had "intimidated" them into withdrawing by serving them with a late-night subpoena to produce—within less than one week—all financial documents, in every format, from any source, over a five-year period. Letter from James and Judy Constance to Administrative Law Judge Elliot, Admin. Proc. No. 3-15006, Doc. No. 38 (Dec. 9, 2012).

Even though SEC ALJs are not authorized to engage in rulemaking, *see* 15 U.S.C. § 78d-1(a), Judge Elliot also concluded that Lucia's use of the word "backtest" was misleading because the slideshow did not "mee[t] the definition of 'backtest' that *I have adopted*," Pet. App. 171a (emphasis added). Lucia's employees testified, and financial industry pamphlets confirmed, that "backtests" can be based partly on assumptions. *See id.* 163a. But Judge Elliot accepted

the Enforcement Division's unprecedented and unsupported position, ruling that a "backtest" can only describe hypotheticals based exclusively on historical data. *Id.* 196a-197a.

Judge Elliot further found, among other things, that the disclosed use of an assumed inflation rate was misleading, Pet. App. 197a, even though attendees knew that the assumed rate "did not reflect" actual rates, *id.* 178a, and the BOM strategy undisputedly would have outperformed the comparison portfolios using *either* rate. Judge Elliot also concluded that Lucia's statement that "the BOM strategy is purely a 'withdrawal strategy'" was "knowingly false," *id.* 205a—which does not make sense because the order instituting proceedings itself had described the BOM strategy as a withdrawal strategy, *see* C.A.D.C. JA4. Moreover, no securities were ever offered or sold at the seminars, and indeed there was no allegation that Lucia had engaged in fraudulent securities trading.

There was no evidence, much less a finding, that the conduct at issue caused *any* investor losses. *See* Pet. App. 101a. Nevertheless, Judge Elliot imposed monetary sanctions based on "the substantial financial success" Lucia and his company had purportedly "enjoyed at their clients' expense." *Id.* 231a. In addition, Judge Elliot barred Lucia from working as an investment adviser or associating with broker-dealers (including his own son) for the rest of his life, *id.* 225a-233a, in keeping with his established practice of "never giv[ing] less than a permanent bar" as a sanction against an investment adviser in a contested proceeding, Transcript at 103:20, *In re W. Pac. Capital Mgmt.*, Admin. Proc. No. 3-14619 (Apr. 2, 2012). As a result of this proceeding, Ray Lucia is unemployable

in his lifelong profession and on the verge of bankruptcy.

4. Lucia timely sought Commission review, challenging the initial decision on the merits and arguing that Judge Elliot held office in violation of the Appointments Clause. Pet. App. 38a-40a. The Commission granted discretionary review and—by a 3-2 vote—affirmed in relevant part. *Id.* 39a-40a, 110a.

On the merits, the Commission majority sustained Judge Elliot's conclusion that the presentations were misleading because a "backtest" must use "historical data" whereas Lucia's hypotheticals used disclosed assumptions in addition to historical data. Pet. App. 66a-69a. Relying on *Landry* v. *FDIC*, 204 F.3d 1125 (D.C. Cir. 2000), the Commission majority further concluded that SEC ALJs are "not subject to the requirements of the Appointments Clause," Pet. App. 86a, because "it is 'the Commission's issuance of a finality order' that makes [an ALJ's] decision effective and final," *id.* 90a.

In the SEC's only written dissent of 2015, Commissioners Gallagher and Piwowar sharply disagreed on the merits. *See* Pet. App. 110a-114a. The dissenters explained that the majority had "create[d] from whole cloth specific requirements for advertisements that include the word 'backtest,'" and then deemed it misleading "if a backtest fails to use actual historical rates—even if the slideshow presentation specifically discloses the use of assumed rates for certain components." *Id.* 111a. The dissenters also noted that Article III courts should decide the Appointments Clause issue. *Id.* 113a.

5. A three-judge panel of the D.C. Circuit denied Lucia's timely petition for review. Pet. App. 4a. In

addition to sustaining the liability and sanctions orders on the merits, *id.* 21a-36a, the panel rejected the Appointments Clause challenge.

The panel stated that, under the D.C. Circuit's 2-1 decision in *Landry*, the constitutional "analysis begins, and ends," with "whether Commission ALJs issue final decisions of the Commission." Pet. App. 13a. According to the panel, the Commission's power of discretionary review was sufficient to render its ALJs mere employees. *Id.* 13a-16a. Lucia argued that *Landry*'s approach was incompatible with this Court's decisions in *Freytag* and *Edmond*, but the panel summarily responded that "this court has rejected that argument, and *Landry* is the law of the circuit." *Id.* 13a.

The Tenth Circuit subsequently ruled that SEC ALJs *are* Officers, *Bandimere* v. *SEC*, 844 F.3d 1168, 1179, 1188 (10th Cir. 2016), expressly disagreeing with the D.C. Circuit's reasoning in this case and in *Landry*. In the Tenth Circuit's view, the D.C. Circuit "place[d] undue weight on final decision-making authority." *Id.* at 1182.

The D.C. Circuit granted rehearing en banc, Pet. App. 245, but—after full briefing and argument—issued a brief *per curiam* order stating that the petition for review was denied by an equally divided court, *id.* 1a-2a. That order left the panel decision intact. *See* D.C. Cir. R. 35(d).

6. In response to Lucia's petition for a writ of certiorari, the Solicitor General acknowledged that SEC ALJs exercise "'significant authority pursuant to the laws of the United States,'" and are therefore Officers. U.S. Cert. Br. 10, 12 (quoting *Buckley*, 424 U.S. at 126). This Court granted certiorari and appointed an *amicus curiae* to defend the judgment below.

SUMMARY OF ARGUMENT

The Appointments Clause prescribes the means of appointing every "Office[r] of the United States." U.S. Const. art. II, § 2, cl. 2. SEC ALJs are Officers because they exercise significant authority under federal law, yet they indisputably are not appointed in conformity with the Clause. Because Lucia was tried before an unconstitutional tribunal, a meaningful remedy is required.

I. SEC ALJs, who preside over adversarial enforcement proceedings, easily fit the Appointments Clause's expansive conception of "Officer."

A. The text and purpose of the Appointments Clause confirm that the category of "Officers" is intentionally broad. *Any* official whose position is "'established by Law'" and who exercises "significant authority" under federal law is an Officer. *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam) (citation omitted). Applying this definition, this Court has consistently held that federal adjudicators who preside over adversarial enforcement proceedings are Officers.

B. SEC ALJs are Officers because their position is established by federal law, *see, e.g.*, 5 U.S.C. §§ 556-57, and they preside over adversarial enforcement proceedings. SEC ALJs perform all of the same discretionary functions that this Court found "significant" in *Freytag* v. *Commissioner*, 501 U.S. 868, 881-82 (1991)—and then some. Under a straightforward application of *Freytag*, SEC ALJs are Officers.

C. Relying on D.C. Circuit precedent, the panel below concluded that SEC ALJs are not Officers because their decisions are subject to discretionary review by the Commission. *This* Court's precedents make clear, however, that "authority to enter a final

decision" is not essential to Officer status, *Freytag*, 501 U.S. at 881; indeed, authority to enter decisions subject to discretionary review is one of the hallmarks of inferior (as contrasted with principal) Officers, *Edmond* v. *United States*, 520 U.S. 651, 665 (1997).

D. Congress provided, in both the securities laws and the APA, that ALJs are "officers." That designation is all but dispositive of their status under the Appointments Clause. *See United States* v. *Germaine*, 99 U.S. 508, 510 (1879). This statutory scheme also destroys any suggestion that ALJs should be considered employees, rather than Officers, to preserve "adjudicatory independence." Congress authorized SEC enforcement actions to proceed either in Article III courts, which are independent of the Commission, or before SEC ALJs, which are not. By pretending that its ALJs are "independent" adjudicators, the SEC evades the "public accountability" that the Appointments Clause requires. *Edmond*, 520 U.S. at 660.

II. The constitutional violation in this case requires an appropriate and commensurate remedy.

A. Lucia is constitutionally entitled to, at minimum, a new "hearing before a properly appointed" adjudicator. *Ryder* v. *United States*, 515 U.S. 177, 188 (1995); *see also United States* v. *L.A. Tucker Truck Lines, Inc.*, 344 U.S. 33, 36 (1952). An entirely new proceeding is required because a defect in "the appointment" of the adjudicator "goes to the validity" of the underlying proceeding, *Freytag*, 501 U.S. at 879, and is a structural error that "affect[s] the ... whole adjudicatory framework," *Williams* v. *Pennsylvania*, 136 S. Ct. 1899, 1910 (2016).

B. The Commission has already announced that SEC ALJs may "ratify" decisions made when they had

no constitutional authority to act. That is a misuse of ratification principles, *see FEC* v. *NRA Political Victory Fund*, 513 U.S. 88, 98-99 (1994); indeed, ratification in this context is indistinguishable from the "*de facto* officer" doctrine rejected by this Court in *Ryder*, 515 U.S. at 179. To send a clear message that the Appointments Clause is no mere "matter of 'etiquette or protocol,'" *Edmond*, 520 U.S. at 659 (citation omitted), and to avoid another trip up the appellate ladder, this Court should order outright dismissal of this proceeding.

ARGUMENT

In recent years, the Securities and Exchange Commission has shifted more than 80% of its enforcement proceedings to its in-house tribunal, *see* Jean Eaglesham, *SEC Wins With In-House Judges* ("*SEC Wins*"), Wall St. J. (May 6, 2015), http://tinyurl.com/o9vsozr, where its administrative law judges preside over adversarial proceedings and issue decisions that almost always become the Commission's final word. The Enforcement Division has fared well in this captive forum, winning over 90% of the time. *Ibid.* Contemporaneously with this case, the Enforcement Division won an astonishing 219 cases in a row, *see* Ryan Jones, *The Fight over Home Court: An Analysis of the SEC's Increased Use of Administrative Proceedings*, 68 SMU L. Rev. 507, 509 (2015), including 50 of its first 50 cases tried before ALJ Elliot, who conducted this proceeding, *see* Sarah N. Lynch, *SEC Judge Who Took on the "Big Four" Known for Bold Moves* ("*SEC Judge*"), Reuters (Feb. 3, 2014), http://tinyurl.com/hlu76fl.

The Commission's administrative tribunal violates a "significant structural safeguar[d] of the constitutional scheme." *Edmond* v. *United States*,

520 U.S. 651, 659 (1997). The Appointments Clause of Article II prescribes the means for appointing any "Office[r] of the United States." U.S. Const. art. II, § 2, cl. 2. As the Solicitor General now concedes, SEC ALJs are Officers because they exercise significant authority under federal law. U.S. Cert. Br. 14-15. The Commission, however, has refused to appoint its ALJs in a manner that comports with the Appointments Clause. Pet. App. 87a. Indeed, the Commission promotes its ALJs as "independent" adjudicators even though Congress made them subordinates of the Commission who carry out executive policy.

Granting the petition for review in this proceeding, and imposing a meaningful remedy for the Commission's unrepentant violation of Lucia's constitutional rights, will be important steps toward bringing our Executive Branch back in line with the Framers' design.

I. SEC ALJs Are Officers Of The United States

The Framers considered "'the power of appointment to offices'" to be "'the most insidious and powerful weapon of eighteenth century despotism.'" *Freytag* v. *Comm'r*, 501 U.S. 868, 883 (1991) (citation omitted). To prevent the "'manipulation of official appointments,'" *ibid.* (citation omitted), the Framers "carefully husband[ed] the appointment power" to "limit its diffusion," *id.* at 883, and to ensure that "*all ... officers* of the Union, will ... be the choice, though a remote choice, of the people themselves," The Federalist No. 39, at 271 (James Madison) (Cynthia B. Johnson ed., 2006) (emphasis added).

Principal Officers—such as ambassadors, judges, and department heads—must be appointed by the

President "by and with the Advice and Consent of the Senate." U.S. Const. art. II, § 2, cl. 2. Congress may, however, "vest the Appointment of such inferior Officers ... in the President alone, in the Courts of Law, or in the Heads of Departments." *Ibid.* "Unless their selection is elsewhere provided for" in the Constitution—as with the President himself—*every* federal official whose position is "'established by Law'" and who exercises "significant authority" must be appointed under the Appointments Clause. *Buckley* v. *Valeo*, 424 U.S. 1, 118, 126, 132 (1976) (per curiam) (citation omitted).

For years, no one (including government counsel) seemed to know how SEC ALJs were selected; only during recent litigation, and in response to a discovery order from a federal judge, did the Commission disclose that its ALJs are "hired" by its Chief Administrative Law Judge from a list of three candidates identified by the Office of Personnel Management. Pet. App. 296a-297a. It is not disputed that this hiring process is not consonant with the Appointments Clause. U.S. Cert. Br. 19; Pet. App. 87a. As Judge Elliot recently acknowledged, "if in fact I am an officer, then I would not hold my position lawfully." Transcript at 6:14-16, *In re David S. Hall*, Admin. Proc. No. 3-17228 (Dec. 20, 2017).

Article II and this Court's precedents make clear that the category of constitutional "Officers" is purposefully broad and includes adjudicators who decide the rights of citizens under federal law. SEC ALJs are Officers because they preside over adversarial enforcement proceedings in which they take testimony, rule on the admissibility of evidence, conduct trials, and enforce compliance with their orders. The panel's

approach, which would exempt from the Appointments Clause all officials without final decision-making authority, cannot be reconciled with this Court's precedents. And by treating its ALJs as though they were independent adjudicators, the Commission has evaded the very accountability the Clause was designed to ensure.

A. The Category Of Constitutional Officers Is Expansive

This Court has consistently applied a simple, sweeping definition of "Officer": *Every* official whose position is "'established by Law'" and who exercises "significant authority pursuant to the laws of the United States is an 'Officer of the United States,' and must, therefore, be appointed in the manner prescribed by" the Appointments Clause. *Buckley*, 424 U.S. at 125-26 (quoting U.S. Const. art. II, § 2, cl. 2).

1. *Buckley*'s broad definition of "Officer" makes perfect sense of the constitutional text and purpose and two centuries of this Court's precedents.

The Clause's text is intentionally inclusive. *See* 2 Samuel Johnson, *A Dictionary of the English Language*, s.v. "officer" (6th ed. 1785) ("A man employed by the publick"); 2 Noah Webster, *An American Dictionary of the English Language*, s.v. "officer" (1828) ("A person commissioned or authorized to perform any public duty"); *see also* William Blackstone, 3 *Commentaries on the Laws of England* 327-46 (1765) ("officer" refers to, among other persons, "sheriffs; coroners; justices of the peace; constables; surveyors of highways; and overseers of the poor"). Indeed, historical evidence suggests an even broader meaning, "encompass[ing] any individual who had ongoing responsibility for a governmental duty." Jennifer L. Mascott,

Who Are 'Officers of the United States'?, 70 Stan. L. Rev. (forthcoming 2018) (manuscript at 8).

A broad construction of "Officer," furthermore, is crucial to the "structural safeguar[d]" the text provides. *Edmond*, 520 U.S. at 659. The Framers "understood ... that by limiting the appointment power" to those who were readily identifiable, "they could ensure that those who wielded it were accountable to political force and the will of the people." *Freytag*, 501 U.S. at 884. An unduly narrow definition of Officer would invite precisely the sort of "diffusion of the appointment power" that the Clause was designed to prevent. *Id.* at 878.

Buckley's broad definition of "Officer" also reflects two centuries of decisions holding a wide range of officials to be subject to the Clause—including:

- district-court clerks, *Ex parte Hennen*, 38 U.S. (13 Pet.) 230, 258 (1839);
- a clerk to an assistant treasurer in Boston, *United States* v. *Hartwell*, 73 U.S. (6 Wall.) 385, 393-94 (1868);
- engineers and assistant surgeons, *United States* v. *Perkins*, 116 U.S. 483, 484 (1886); *United States* v. *Moore*, 95 U.S. 760, 762 (1878);
- "thousands of clerks in the Departments of the Treasury, Interior and the othe[r]" departments, *United States* v. *Germaine*, 99 U.S. 508, 511 (1879), responsible for "the records, books, and papers appertaining to the office," *Hennen*, 38 U.S. (13 Pet.) at 259;
- judges of election and federal marshals, *Ex parte Siebold*, 100 U.S. 371, 397-99 (1880);

- "commissioners of the circuit courts" who "t[ook] ... bail for the appearance of persons charged with crime," *United States* v. *Allred*, 155 U.S. 591, 594 (1895);
- extradition commissioners, *Rice* v. *Ames*, 180 U.S. 371, 378 (1901);
- district-court commissioners, *Go-Bart Importing Co.* v. *United States*, 282 U.S. 344, 352-54 (1931); and
- U.S. attorneys, *Myers* v. *United States*, 272 U.S. 52, 159 (1926).

Only individuals with "no general functions, nor any employment which has any duration as to time," whose posts lack "tenure, duration, continuing emolument, or continuous duties," and who "ac[t] only occasionally and temporarily" have been held by this Court to be employees who fall outside the Clause. *Auffmordt* v. *Hedden*, 137 U.S. 310, 327 (1890); *see also Buckley*, 424 U.S. at 126 n.162 ("employees" are "lesser functionaries subordinate to" Officers).

2. This Court's post-*Buckley* cases confirm that non-Article III adjudicators—who pass upon the rights of citizens in contested proceedings under federal law—are Officers because they wield significant federal authority, regardless of whether their decisions are subject to review by a superior Officer. Since the Founding, this Court has *never* found a federal adjudicator who presides over adversarial proceedings to be a mere employee exempt from the Clause—while finding a wide range of quasi-judicial officials to be Officers.

The critical decision is *Freytag*, in which this Court held that special trial judges ("STJs") of the

U.S. Tax Court were Officers because they held positions "'established by Law'" and exercised authority "so 'significant' that it was inconsistent with the classifications of ... employees." 501 U.S. at 880-82 (citation omitted). STJs could make final decisions in some cases; but in other cases (including *Freytag* itself) they lacked final decision-making power and could issue only proposed opinions, which the Tax Court was free to accept or reject. *Id.* at 882. Even when they could not enter final decisions, this Court unanimously held, STJs acted as Officers because they "exercised significant discretion" in performing "important functions"—specifically, "tak[ing] testimony," "conduct[ing] trials," "rul[ing] on the admissibility of evidence," and "enforc[ing] compliance with discovery orders." *Id.* at 881-82; *accord id.* at 901 (Scalia, J., concurring in part and concurring in the judgment). And when STJs could enter final decisions, that was an independent reason why they were Officers. *Id.* at 882 (majority op.).

This Court has since held that military judges, too, are Officers based on their significant adjudicatory duties. In *Weiss* v. *United States*, 510 U.S. 163 (1994), the Court explained that military trial and appellate judges are Officers "because of the authority and responsibilities [they] possess," which include ruling on procedural and legal issues and adjudicating offenses under the Uniform Code of Military Justice. *Id.* at 167-69. In *Edmond*, the Court recognized that intermediate appellate military judges are Officers, in part because they "independently 'weigh the evidence, judge the credibility of witnesses, and determine controverted questions of fact.'" 520 U.S. at 662 (quoting 10 U.S.C. § 866(c)). They also could enter "a final decision on behalf of the United States" when "permitted to do so by other Executive officers." *Id.* at 665; *see*

also Ryder v. *United States*, 515 U.S. 177, 180-88 (1995).

Over the years, the Court has considered a variety of quasi-judicial officials—including clerks, commissioners, and non-Article III judges—and held that *all* of them are Officers. *See generally* Mascott, *supra*; Kent Barnett, *Resolving the ALJ Quandary*, 66 Vand. L. Rev. 797, 799-803, 810-14 (2013). For example, court commissioners (the predecessors of today's magistrate judges) are constitutional Officers at least in part based on their adjudicatory functions in adversarial proceedings. *Go-Bart*, 282 U.S. at 353 n.2 (commissioners "take oaths and acknowledgments" and "take recognizances from witnesses on preliminary hearings"); *Allred*, 155 U.S. at 595 (commissioners "sit as judge or arbitrator ... between the captains and crews of ... vessels" and "take testimony and proofs of debt in bankruptcy proceedings").

Like all these other federal adjudicators, SEC ALJs are Officers within the meaning of the Appointments Clause.

B. SEC ALJs Have All The Characteristics Of Officers

It is not reasonably debatable that SEC ALJs hold offices established by law, or that they exercise authority—including ruling on the admissibility of evidence, taking testimony, and conducting trials—previously deemed sufficiently "significant" to confer Officer status. *Freytag*, 501 U.S. at 881-82. This Court need go no further to conclude that SEC ALJs are Officers.

1. Offices Established By Law

The positions held by SEC ALJs are indisputably "'established by Law.'" *Freytag*, 501 U.S. at 881 (citation omitted); *Bandimere* v. *SEC*, 844 F.3d 1168, 1179 (10th Cir. 2016). Like the STJs in *Freytag*, SEC ALJs' "duties, salary, and means of appointment" are all "specified by statute." 501 U.S. at 881; *see* 5 U.S.C. §§ 556-57 (establishing ALJs' position and powers in hearings); *id.* § 5372 (establishing salaries); *id.* § 3105 (establishing hiring practices). Commission regulations further define SEC ALJs' powers. *See, e.g.*, 17 C.F.R. §§ 200.14, 201.111. An ALJ's position is also not "temporary," *Freytag*, 501 U.S. at 881; ALJs "receiv[e] a career appointment," 5 C.F.R. § 930.204(a), and may be removed only for cause, *see* 5 U.S.C. § 7521(a). There can be no serious dispute that SEC ALJs hold offices established by law.

2. Significant Federal Authority

SEC ALJs also unquestionably "'exercis[e] significant authority pursuant to the laws of the United States.'" *Freytag*, 501 U.S. at 881 (quoting *Buckley*, 424 U.S. at 126); *see Bandimere*, 844 F.3d at 1178, 1188 (table summarizing SEC ALJs' duties and showing they "carry out 'important functions'" and "'exercis[e] significant authority'"). The Commission has endowed its ALJs with a litany of substantive and procedural powers that require the exercise of broad discretion and closely parallel the authority of the STJs in *Freytag*.

a. In overseeing SEC administrative hearings, ALJs exercise authority over a wide range of matters at every stage of the case, including:

- amending charging documents, 17 C.F.R. § 201.200(d)(2);

- entering orders of default, *id.* § 201.155;
- consolidating proceedings, *id.* § 201.201(a);
- "[a]dminister[ing] oaths and affirmations," *id.* §§ 200.14(a)(1), 201.111(a);
- "[i]ssu[ing] subpoenas," *id.* §§ 200.14(a)(2), 201.111(b);
- ordering depositions and acting as the "deposition officer," *id.* §§ 201.233-.234;
- ordering production of evidence and regulating document production, *id.* §§ 201.111(b), .230, .232;
- issuing protective orders, *id.* § 201.322;
- "[r]ul[ing] upon motions," including for summary disposition, *id.* §§ 200.14(a)(7), 201.111(h), .250;
- rejecting filings for procedural noncompliance, *id.* § 201.180(b);
- granting extensions of time and stays, *id.* § 201.161;
- "[h]old[ing] pre-hearing conferences" and "requir[ing]" attendance at such conferences, *id.* §§ 200.14(a)(6), 201.111(e), .221(b);
- ordering prehearing submissions, *id.* § 201.222(a);
- "[r]egulat[ing] the course of [the] hearing," *id.* §§ 200.14(a)(5), 201.111(d);
- receiving "relevant evidence" and ruling upon admissibility, *id.* § 201.111(c);
- "[r]ul[ing] on offers of proof," *id.* §§ 200.14(a)(3), 201.111(c);

- "[e]xamin[ing] witnesses," *id.* § 200.14(a)(4);
- regulating the scope of cross-examination, *id.* § 201.326;
- regulating "the conduct of the parties and their counsel," *id.* § 201.111(d); and
- imposing sanctions for "contemptuous conduct," *id.* § 201.180(a).

As the Tenth Circuit recognized, "STJs and ALJs closely resemble one another where it counts." *Bandimere*, 844 F.3d at 1187. Like the STJs that this Court addressed in *Freytag*, SEC ALJs "take testimony," "conduct trials," "rule on the admissibility of evidence," "enforce compliance with discovery orders," and otherwise perform "more than ministerial tasks." 501 U.S. at 881-82. To be sure, SEC ALJs cannot impose fines or imprisonment for contempt. But that is true of most administrative agency officials, *see ICC* v. *Brimson*, 154 U.S. 447, 488-89 (1894), including STJs, *see* 26 U.S.C. § 7456(c).

b. In addition to performing the same functions found significant in *Freytag* (and then some), SEC ALJs "prepare an initial decision containing the conclusions as to the factual and legal issues presented," 17 C.F.R. §§ 200.14(a)(8), 201.111(i), .141(b), .360(a), in which the ALJ "publicly states whether respondents have violated securities laws and imposes penalties for violations," *Bandimere*, 844 F.3d at 1180 n.25. If no timely petition for review is filed or if the Commission declines review, the ALJ's initial decision by statute "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. § 78d-1(c); *accord* 5 U.S.C. § 557(b) (ALJs' "initial decisions" automatically become final "without further proceedings" absent further review).

On the relatively rare occasions the Commission *does* review an ALJ's initial decision, the Commission does not review the decision anew, but defers to the ALJ's credibility determinations and factual findings. *See In re Clawson*, Exchange Act Release No. 48,143, 2003 WL 21539920, at *2 (July 9, 2003) ("We accept [an SEC ALJ's] credibility finding, absent *overwhelming evidence* to the contrary" (emphasis added)); *In re Bridge*, Securities Act Release No. 9,068, 2009 WL 3100582, at *18 n.75 (Sept. 29, 2009) (similar). Because the Commission views its ALJs as "'in the best position to make findings of fact ... and resolve any conflicts in the evidence,'" Pet. App. 241a (citation omitted), the Commission relies heavily, if not solely, on their findings and determinations.

c. This case is a prime illustration of how SEC ALJs exercise significant authority in shaping the record. As the Commission emphasized, SEC ALJs play a "vital role" in the adjudicative process. Pet. App. 241a. The Commission even remanded the case to Judge Elliot for additional factual findings, *id.* 239a, because those findings were "a matter of considerable importance" to the Commission, *id.* 241a. Judge Elliot was the only adjudicative official in this entire proceeding who saw and heard the witnesses testify, who reviewed all the evidence, and who directly and irrevocably shaped the record through evidentiary and other rulings. A different adjudicator neutrally exercising the same discretion could easily have decided the case in Lucia's favor, or declined to impose a permanent bar.

Judge Elliot exercised federal authority in developing the factual basis for the liability and sanctions orders. Despite relying heavily on the testimony of

two audience members on the critical issue of materiality, Judge Elliot made it nearly impossible for Lucia to challenge, or the Commission meaningfully to review, his shaky credibility determinations. For example, although one witness had admitted to filing a false claim against Lucia, Judge Elliot excluded evidence related to that false claim, so there was "no evidence" in the record to controvert his credibility determination. Pet. App. 193a. The Commission consequently deferred to Judge Elliot's findings based on the witnesses' testimony. *See id.* 69a-70a.

Judge Elliot's exercise of federal authority extended to legal issues as well. Most saliently, the Commission—by a 3-2 vote—sustained Judge Elliot's determination that Lucia's presentations were misleading because their use of the word "backtest" did not "mee[t] the definition of 'backtest' that [Judge Elliot] ha[d] adopted." Pet. App. 171a. Judge Elliot's definition, however, had been "create[d] from whole cloth." *Id.* 111a (dissenting op.). Despite the lack of any preexisting statutory or regulatory definition of the term, and even though Lucia offered industry examples of "backtests" that were not based exclusively on historical data, *id.* 52a-53a (majority op.), the Commission validated Judge Elliot's rulemaking-by-opinion by adopting his definition wholesale, *id.* 66a.

Although Lucia petitioned for judicial review of the liability and sanctions orders, the D.C. Circuit panel began its merits discussion with the observation that "[o]ur review is deferential," Pet. App. 22a—and then proceeded to defer to the Commission, *id.* 26a-32a, 33a, 35a, which in turn had relied extensively on Judge Elliot's findings and credibility determinations, *e.g.*, *id.* 40a, 62a-64a, 69a-70a. An unconstitutional official thus established both the legal and factual

predicates for the ensuing actions of the SEC and the court of appeals—including the lifetime bar imposed on Lucia.

* * *

The authority of SEC ALJs mirrors that of the STJs in *Freytag*, as well as the military judges in *Weiss* and *Edmond*. Under this Court's established (and unbroken) line of Appointments Clause jurisprudence, SEC ALJs are Officers because they adjudicate adversarial enforcement proceedings. *That* should begin, and end, the analysis.

C. The D.C. Circuit Panel Erred In Holding That SEC ALJs Are Not Officers

Without addressing the many important and discretionary duties exercised by SEC ALJs, the panel held that, under D.C. Circuit precedent, the "analysis begins, and ends," with whether SEC ALJs can issue unreviewable final decisions of the Commission, and concluded that they cannot. Pet. App. 13a. The panel further refused to distinguish that precedent based on the level of deference the Commission affords its ALJs. *Id.* 18a-19a. This Court's precedents make clear, though, that authority to issue final decisions is not a prerequisite of Officer status, and the standard of review simply is "not relevant" to the analysis. *Freytag*, 501 U.S. at 874 n.3.

1. Final Decision-Making Authority

The panel uncritically relied on a previous decision in which a divided panel of the D.C. Circuit had held that Officers must have the "power of final decision." *Landry* v. *FDIC*, 204 F.3d 1125, 1134 (D.C. Cir. 2000); *see* Pet. App. 13a. Confining the Appointments Clause's reach to officials invested with the power of

final decision, however, contravenes this Court's teaching in *Freytag*. At minimum, confining the Clause's reach to those who can issue *unreviewable* final decisions cannot be reconciled with this Court's teaching in *Edmond*. As this Court has explained, the authority to issue final decisions distinguishes inferior Officers from principal Officers; it is not, and cannot be, a *sine qua non* for the Clause to apply at all. Regardless, SEC ALJs can and do enter decisions that become final with—or without—the possibility of Commission review.

a. *Freytag* expressly rejected the argument that inability to make final decisions takes officials outside the Appointments Clause. 501 U.S. at 880-82. In many cases, including *Freytag* itself, STJs "lack[ed] authority to enter a final decision," and merely "assist[ed]" the Tax Court "in taking the evidence and preparing the proposed findings and opinion." *Id.* at 880-81. *Freytag* held that deeming those adjudicators mere employees on that basis would "ignor[e] the significance of the duties and discretion that [the] judges possess[ed]"—namely, that they "perform[ed] more than ministerial tasks," including "tak[ing] testimony," "conduct[ing] trials," and "rul[ing] on the admissibility of evidence." *Id.* at 881-82.

To be sure, the *Freytag* Court reasoned that "*[e]ven if* the duties of special trial judges ... were not as significant as we ... have found them to be, our conclusion would be unchanged" because STJs could issue final decisions in *other* cases. 501 U.S. at 882 (emphasis added). But that "unchanged" "conclusion" (*i.e.*, holding) was that STJs' duties and discretion render them Officers, even when they cannot enter final decisions. *See id.* at 881-82. Indeed, this Court expressly "agree[d]," *id.* at 881, with a Second Circuit

decision that had held that STJs are Officers because they "exercise a great deal of discretion and perform important functions" even in cases where "the ultimate decisional authority ... rests with the Tax Court judges." *Samuels, Kramer & Co.* v. *Comm'r*, 930 F.2d 975, 985 (2d Cir. 1991).

The D.C. Circuit is the only appellate court to have misread *Freytag* as imposing a requirement of final decision-making authority as a prerequisite to Officer status. *See Burgess* v. *FDIC*, 871 F.3d 297, 301 (5th Cir. 2017) (*Freytag*'s "additional statement—that [STJs'] duties and discretion, coupled with the power to enter final judgments also makes the STJs Officers—was dicta or an alternative basis for its decision"); *Bandimere*, 844 F.3d at 1184 (*Freytag* "did not make final decision-making power the essence of inferior officer status"); *see also Landry*, 204 F.3d at 1142 (Randolph, J., concurring in part and concurring in the judgment) (*Freytag*'s discussion of final decision-making authority was "clearly designated ... as an alternative holding").

The D.C. Circuit's reading is not only unique; it is also wrong. Time and again, this Court has held that adjudicators who lacked final decision-making authority nevertheless were constitutional Officers. *See, e.g.*, *Go-Bart*, 282 U.S. at 352, 354 ("All the [commissioner's] acts ... were preparatory and preliminary to a consideration of the charge by a grand jury and ... the final disposition of the case in the district court"); *Allred*, 155 U.S. at 595 (commissioners are "subject to the orders and directions of the court appointing them"); *accord Weiss*, 510 U.S. at 168 ("No sentence imposed [by the military trial judge] becomes final until it is approved by the officer who convened the court-martial"). The approach taken by the D.C.

Circuit, in *Landry* and the panel decision in this case, cannot be reconciled with these precedents.

b. The panel further erred by holding that officials whose decisions *can and do* become the agency's final word are not Officers, so long as their decisions are subject to "discretionary review" by principal Officers. Pet. App. 16a. That holding conflicts with this Court's decision in *Edmond*.

Edmond held that judges on the Coast Guard Court of Criminal Appeals were inferior Officers because their decisions were always subject to further discretionary review by principal Officers—namely, the Court of Appeals for the Armed Forces—whether by *sua sponte* order of the Judge Advocate General or where the CAAF exercised its discretion to grant review. 520 U.S. at 664-65; *see* 10 U.S.C. § 867(a). This lack of "power to render a final decision ... unless permitted to do so by other Executive officers," *Edmond* explained, is the defining *feature* of "'inferior officers.'" 520 U.S. at 663, 665. It did not render the adjudicators mere employees.

Here, too, this Court has repeatedly held that officials who cannot render an unreviewable final decision of the Executive Branch are nevertheless Officers:

- district-court commissioners, *Go-Bart*, 282 U.S. at 352, 354;
- circuit-court commissioners, *Allred*, 155 U.S. at 594-95;
- military trial and appellate judges, *Weiss*, 510 U.S. at 168-69;

- judges of the Coast Guard Court of Military Review, *Ryder*, 515 U.S. at 180-88; *Edmond*, 520 U.S. at 653, 665;
- judges of the Coast Guard Court of Criminal Appeals, *Edmond*, 520 U.S. at 662-66;
- members of the Public Company Accounting Oversight Board, *Free Enter. Fund* v. *PCAOB*, 561 U.S. 477, 486 (2010); *see also Free Enter. Fund* v. *PCAOB*, 537 F.3d 667, 673 (D.C. Cir. 2008).

None of these officials would be Officers under the D.C. Circuit's finality test, yet this Court has held that *all* of them are.

The D.C. Circuit's finality test would even exclude federal magistrate judges, who, like SEC ALJs, have power to issue decisions that can become final, 28 U.S.C. § 636(b)(1)(C); make evidentiary rulings, *id.* § 636(b)(1)(B); and preside over trials, *id.* § 636(a)(3). Although magistrate judges cannot (absent consent) render unreviewable final decisions on the merits, *id.* § 636(b)(1)(A), there is no question but that their ability to shape the evidentiary record is alone sufficient to render them Officers. *Cf. Butz* v. *Economou*, 438 U.S. 478, 513 (1978) ("[T]he role of the ... administrative law judge ... is 'functionally comparable' to that of a judge.... He may issue subpoenas, rule on proffers of evidence, regulate the course of the hearing, and make or recommend decisions."). SEC ALJs are Officers for at least the same reason.

Officers do not need to possess the authority to issue unreviewable final decisions. "The question," as the Office of Legal Counsel has explained, "is simply whether a position possesses delegated sovereign authority to act in the first instance, whether or not that

act may be subject to direction or review by superior officers." *Officers of the United States Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73, 75 (2007). SEC ALJs indisputably fit that description.

c. The D.C. Circuit's finality rule confuses the distinction between inferior and principal Officers with the distinction between Officers and employees. As *Edmond* explained, the very term "'inferior officer' connotes a relationship with some higher ranking officer"; their "work is directed and supervised" by such "'principal officer[s].'" 520 U.S. at 662-63. *Edmond* emphasized that the lack of "power to render a final decision ... unless permitted to do so by other Executive officers" thus distinguishes "'inferior officers'" from the "'principal officer[s]'" who supervise them. *Id.* at 663, 665; *see also Dep't of Transp.* v. *Ass'n of Am. R.Rs.*, 135 S. Ct. 1225, 1239 (2015) (Alito, J., concurring) ("Inferior officers can do many things, but nothing final should appear in the Federal Register unless a Presidential appointee has at least signed off on it").

By treating a defining feature of inferior Officers as a basis for *exempting* officials from the Appointments Clause, the D.C. Circuit's approach subverts the Framers' design. Article II provides for execution of the laws by the President, aided by principal Officers *and* a cadre of inferior Officers they direct. The Appointments Clause by its terms covers *both* types of Officers. U.S. Const. art. II, § 2, cl. 2. Under the D.C. Circuit's finality rule, however, only officials with unreviewable final decision-making authority—who primarily if not exclusively will be *principal* Officers—would be subject to the Clause. That approach would remove the Constitution's "structural safeguar[d]" from all first-line adjudicators. *Edmond*, 520 U.S. at

659. Indeed, the D.C. Circuit's finality rule would virtually erase the category of "inferior Officers" from the text of our Constitution.

d. Even if final decision-making authority were necessary to Officer status, SEC ALJs still would be Officers because they can and do enter decisions that become final with—or without—any possibility of Commission review.

To begin, SEC rules "expressly authorize" ALJs to issue default orders to levy "sanctions and to impose cease-and-desist orders via default." *In re Alchemy Ventures, Inc.*, Exchange Act Release No. 70,708, 2013 WL 6173809, at *4 (Oct. 17, 2013) (citing 17 C.F.R. § 201.155(a)). Although the current practice is for ALJs to issue initial decisions in cases of default, the Commission has "emphasize[d]" that its ALJs' prior default orders are valid and judicially "enforceable" without *any* Commission review. *Ibid.*

In about 90% of cases, moreover, the ALJ's initial decision "become[s] final without plenary agency review." *Bandimere*, 844 F.3d at 1180 n.25 (citing 17 C.F.R. § 201.360(d)(2)); *see also* SEC, ALJ Initial Decisions, https://www.sec.gov/alj/aljdec.shtml. Unlike the recommended decisions rendered by some agency adjudicators (including the FDIC ALJs in *Landry*), which have no effect unless affirmatively adopted by the agency, the initial decisions entered by SEC ALJs "becom[e] the decision of the agency" as a matter of course unless overturned on appeal. 5 U.S.C. § 557(b); U.S. Dep't of Justice, *Attorney General's Manual on the Administrative Procedure Act*, 82-83 (1947) (stating that an "initial decision *will become the agency's final decision* in the absence of an appeal to or review by the agency" (emphasis added)).

When no petition for review is filed with the Commission, "the agency may simply enter an order stating an initial decision is final *without engaging in any review*." *Bandimere*, 844 F.3d at 1184 n.36 (emphasis added). In such cases, the Commission's regulations provide that it "will issue an order that the [ALJ's] decision has become final." 17 C.F.R. §§ 201.360(a)(1), .360(d)(2). The finality order is non-discretionary and issues as a matter of course after 42 days when no petition for review has been filed. *See id.* §§ 201.360(d)(2), .410(b), .411(c); *see also, e.g.*, *In re Horizon Wimba, Inc.*, Exchange Act Release No. 75,929, 2015 WL 5439958, at *1 (Sept. 16, 2015) ("The time for filing a petition for review ... has expired. No such petition has been filed ... , and the Commission has not chosen to review the decision .... Accordingly ... the initial decision ... has become the final decision of the Commission."). And even when review is sought, "[t]he Commission may decline to review any [ALJ] decision." 17 C.F.R. § 201.411(b)(2); *see also In re Bellows*, Exchange Act Release No. 40,411, 1998 WL 611766 (Sept. 8, 1998) (declining review of an initial decision).

Because SEC ALJs can enter default judgments and initial decisions that "become final without any review or revision from an SEC Commissioner," *Bandimere*, 844 F.3d at 1187, they are Officers even under the D.C. Circuit's crabbed view of the Appointments Clause.

2. Standard Of Review

The Tax Court's standard of review was "not relevant to [the Court's] grant of certiorari" in *Freytag*, 501 U.S. at 874 n.3, and the Court ascribed no significance to the deference afforded to STJs, *see id.* at 880-82. It would have been remarkable, in fact, if this

Court *had* attributed constitutional significance to the degree of deference an agency applies in reviewing the decisions of those exercising delegated authority. The standard of review often is the agency's own creation. The Tax Court "had discretion to pick whatever standard of review it saw fit" and applied deferential review based on an "internal rule of procedure." *Lardry*, 204 F.3d at 1142 (Randolph, J., concurring in part and concurring in the judgment). Whether the Appointments Clause applies to an adjudicator cannot turn on how thoroughly the agency *chooses* to review the adjudicator's decisions.

Even when the Commission grants review, it affords ALJ credibility findings "considerable weight," *Bandimere*, 844 F.3d at 1193 (Briscoe, J., concurring), accepting them "absent *overwhelming evidence to the contrary*," *Clawson*, 2003 WL 21539920, at *2 (emphasis added). Unsurprisingly, SEC ALJs' rulings are in fact rarely disturbed. The ALJ who presided over Lucia's case, for example, had apparently *never* been reversed by the SEC in more than 50 prior cases. Lynch, *SEC Judge*; *see also* Eaglesham, *SEC Wins* (finding that in a recent four-and-a-half-year period the Commission ruled for the agency in 95% of its cases, including 88% of cases where the underlying conduct was disputed). The Commission's established practice of rubber-stamping ALJ decisions heightens the importance of ensuring that the Commission itself take political accountability for those decisions.

D. Congress Provided That SEC ALJs Are Executive Officers

Congress expressly provided that SEC ALJs are subordinate "officers" of the Commission. The Commission nevertheless touts its in-house judges as "in-

dependent adjudicators" who conduct hearings "similar to federal bench trials." SEC, Office of Administrative Law Judges, https://www.sec.gov/alj. It is misleading—to courts, regulated persons and entities, and the investing public—for the Commission to represent that its captive adjudicators are independent. The Appointments Clause requires the Commission to accept responsibility for its ALJs because they ultimately exercise *executive* power.

1. This Court long ago recognized that the Appointments Clause is triggered when Congress denominates an official an "officer"—because if Congress meant "others than officers as defined by the Constitution, words to that effect would be used, as servant, agent, person in the service or employment of the government." *Germaine*, 99 U.S. at 510. This principle—which complements *Buckley*'s functional test—provides further grounds for rejecting the panel's conclusion that SEC ALJs are mere employees.

a. Both the federal securities laws, which were enacted between 1933 and 1940, and the APA, which was enacted in 1946, specifically recognize ALJs—or, as they were known then, "hearing examiners"—as "officers."

The securities laws repeatedly refer to SEC ALJs as "officers of the Commission." 15 U.S.C. §§ 77u, 78v, 80a-40, 80b-12. Elsewhere in the securities laws, Congress expressly distinguished "officers" and ALJs from mere "employees." *See, e.g.*, *id.* § 717q ("Appointment of officers and employees"); *id.* § 78d-1(a) (delegation of authority to "an administrative law judge ... or an employee"). Because Congress consistently deemed SEC ALJs "officers," it presumably adopted the "settled meaning" of that term. *Beck* v. *Prupis*, 529 U.S. 494, 500-01 (2000).

The APA, as enacted, similarly referred to hearing examiners as "subordinate officers" or "officers" *nine* times. Administrative Procedure Act, Pub. L. No. 79-404, 60 Stat. 237, 241-42 (1946) (deeming hearing examiners "officers," "presiding officers," and "subordinate officers"); Pet. App. 270a-273a. Indeed, Congress *defined* "officer" in the APA as "an individual ... required by law to be appointed in the civil service by" "the President," "a court of the United States," or "the head of an Executive agency" or "military department." 5 U.S.C. § 2104(a)(1). That definition fits hand-in-glove with the Appointments Clause's requirement that inferior Officers be appointed by "the President alone," "the Courts of Law," or "the Heads of Departments." U.S. Const. art. II, § 2, cl. 2; *see also Free Enter. Fund*, 561 U.S. at 512-13 (multimember agency acting collectively can be a "Head of Department").

b. In enacting the APA, "Congress intended to make [ALJs] 'a special class of semi-independent'" yet still "'*subordinate* hearing officers.'" *Ramspeck* v. *Fed. Trial Exam'rs Conference*, 345 U.S. 128, 132 (1953) (emphasis added) (citation omitted). This "'[l]ong settled and established practice,'" *NLRB* v. *Noel Canning*, 134 S. Ct. 2550, 2559 (2014) (alteration in original) (citation omitted), further confirms that SEC ALJs are Officers rather than mere employees.

When the APA was enacted, it was well understood that hearing examiners would be executive Officers. Congress rejected a proposal for the Judicial Conference to appoint hearing examiners because that body was not constitutionally authorized to make appointments—thus recognizing that hearing examiners were Officers. *See Administrative Procedure Act: Legislative History, 79th Congress, 1944-46*, at 42

(1946) ("*Legislative History*"). And the Attorney General opined that hearing examiners were "inferior officers" even though their tenure and compensation were controlled by the Civil Service Commission. *Administrative Procedure Act, Promotion of Hearing Examiners*, 41 Op. Att'y Gen. 74, 79-80 (1951).

When it was debating the APA, Congress was cognizant of concerns that hearing examiners were "mere tools of the agency concerned" because "their compensation and promotion depended upon" performance ratings given by the agency. *Ramspeck*, 345 U.S. at 130-31. Congress concluded, however, that to completely separate agencies' "quasi-judicial functions from [their] purely administrative functions" would "destroy[] the usefulness of such agencies." *Legislative History* 244. Congress thus specifically rejected proposals to make hearing examiners fully independent of the Executive, whether by creating "a completely separate 'examiners' pool,'" *id.* 215, establishing within each agency a "judicial section" "wholly independent of ... executive control," *id.* 242, or creating a separate "administrative court" to hear cases for all agencies, *ibid.* In other words, Congress decided *not* to confer adjudicative independence on these administrative tribunals.

Congress instead gave hearing examiners only limited separation from their agencies with respect to "their tenure and compensation." *Ramspeck*, 345 U.S. at 132 n.2 (citation omitted). In doing so, Congress expanded on then-recent precedent approving certain restrictions on the President's ability to remove "quasi-judicial" officials. *See Humphrey's Executor* v. *United States*, 295 U.S. 602, 629 (1935). It is an interesting question whether ALJs' current two (or three) layers of for-cause protection, *see* 5 U.S.C. §§ 1202(d),

7521(a), are one (or two) more than the separation of powers will tolerate. *See Free Enter. Fund*, 561 U.S. at 507 n.10 (reserving the question). But that question is not presented at this stage of this case, *see* Cert. Reply 9-11, and has no bearing on whether SEC ALJs are Officers in the first place.

In every other significant respect, Congress made hearing examiners—like today's ALJs—subordinate to their respective agencies. To this day, the statutes give agencies control over ALJs' appointment, *see* 5 U.S.C. § 3105; their powers, including procedural rules, *id.* § 556(c), and substantive authority, *id.* § 557(b); and even their removal, subject to a determination of good cause by the Merit Systems Protection Board, *id.* § 7521(a). Agencies also can reverse their ALJs' initial decisions or reject their recommendatory decisions. *Id.* § 557(b). By design, therefore, agencies such as the SEC "direc[t] and supervis[e]" the work of their subordinate ALJs. *Edmond*, 520 U.S. at 663.

2. The securities laws and the APA put to rest any argument that SEC ALJs should be considered employees rather than Officers because they exercise adjudicatory functions. Because ALJs exercise *executive* power, the concept of adjudicatory "independence" is entirely misplaced in this context.

a. Just as nobody would think that the Commission *itself* is an "independent" adjudicator, even though it is statutorily authorized to decide enforcement proceedings, there should be no illusion that its subordinate Officers are "independent," either. Unlike Article III judges, the Commission and its ALJs implement Commission policy and thereby *exercise* executive power, rather than check it.

The Constitution creates a single "safeguard" to protect litigants' "'right to have claims decided by judges who are free from potential domination by other branches of government.'" *CFTC* v. *Schor*, 478 U.S. 833, 848 (1986) (citation omitted). That safeguard is Article III, which provides judges with life tenure and permanent salary to protect their independence from, and ensure their ability to check, the political branches. U.S. Const. art. III, § 1; *see also Schor*, 478 U.S. at 848. But the Constitution provides "no such guaranties" with respect to other adjudicators, *McAllister* v. *United States*, 141 U.S. 174, 187 (1891)—including those in territorial courts, *ibid.*, Article I courts, *Palmore* v. *United States*, 411 U.S. 389, 390 (1973), and administrative agencies, *Schor*, 478 U.S. at 848, 853-55, 858. This is true whether they are called "hearing examiners," "administrative law judges," or anything else.

Even when they act as adjudicators, executive Officers do not check, but exercise executive power. As this Court long ago explained, "administrative duties" that "involv[e] an inquiry into the existence of facts and the application to them of rules of law" are, in a sense, "judicial acts." *Murray's Lessee* v. *Hoboken Land & Improvement Co.*, 59 U.S. (18 How.) 272, 280 (1856). But that does not "bring such matters under the judicial power." *Ibid.*

The Comptroller of the Treasury, for example, originally adjudicated claims involving debts owed to the United States. *See* An Act to Establish the Treasury Department, 1 Stat. 65, 66 (1789). Yet the Comptroller still was "dependent upon the President" because such adjudication was in service of a classically executive function—collecting revenue. 1 Annals of

Congress 635-36 (1789). Similarly, the Court of Customs Appeals adjudicated certain customs cases involving the United States. *Ex parte Bakelite Corp.*, 279 U.S. 438, 458 (1929). But because those claims concerned "the executive administration and application of the customs laws," they could be "committed exclusively to executive officers" subordinate to their superiors. *Ibid.*

Congress gave the Commission a choice of tribunals for enforcing the federal securities laws. If the Commission is willing and able to prove its case before an independent adjudicator, it may bring an action in an Article III district court. *See* 15 U.S.C. § 78u(d). And if the Commission is not prepared to proceed in federal court, it may adjudicate an enforcement action itself or designate one of its ALJs to do so. *Id.* §§ 78u, 78v. What the Commission *cannot* do is have it both ways, reaping the benefits of its in-house tribunal while holding its ALJs out as "independent" adjudicators.

b. A consistent line of OLC opinions has explained that ALJs are Officers whose duties "are generally executive in nature, because the ALJs determine, on a case-by-case basis, the policy of an executive branch agency." *Sec'y of Educ. Review of Admin. Law Judge Decisions*, 15 Op. O.L.C. 8, 14-15 (1991). The ALJs at issue could not enter unreviewable final decisions for the Executive Branch, OLC opined, precisely because "all executive power ... must ultimately be subject to Presidential control." *Id.* at 14; *see also Authority of Educ. Dep't Admin. Law Judges in Conducting Hr'gs*, 14 Op. O.L.C. 1, 3 (1990) (concluding that ALJs' "limited 'independence'" in terms of tenure protection "does not, however, mean that ALJs may disregard agency rules that are binding on them").

In *Freytag*, Justice Scalia (joined by Justices O'Connor, Kennedy, and Souter) confirmed that ALJs "are all *executive* officers." 501 U.S. at 910 (Scalia, J., concurring in part and concurring in the judgment). "Congress *may* commit the sorts of matters administrative law judges ... now handle to Article III courts," Justice Scalia explained, *ibid.*, but when it instead assigns such matters "to traditional executive departments," those tribunals "exercise the executive power, not the judicial power," *id.* at 909. Executive adjudicators therefore *cannot* exercise their power "'independent ... [of] the Executive Branch,'" but must be subject to Executive control. *Id.* at 912.

In *Free Enterprise Fund*, Justice Breyer (joined by Justices Stevens, Ginsburg, and Sotomayor) likewise indicated that ALJs "'are all executive officers.'" 561 U.S. at 542 (Breyer, J., dissenting) (citation omitted). Justice Breyer added that, when the President elects to "regulate through impartial adjudication," "insulation of the adjudicator from removal at will can help him achieve that goal." *Id.* at 522. But like any other executive Officer, the adjudicator otherwise would remain subject to "the President's control." *Id.* at 530; *see also* Transcript of Oral Argument 62, *Dalmazzi* v. *United States*, No. 16-961 (U.S. Jan. 6, 2018) (Breyer, J.) (noting that agencies exercise executive, "not judicial" power when performing "adjudicatory functions in [their] carrying out of executive duties").

The *Free Enterprise Fund* majority reserved the question whether *all* ALJs are "necessarily" Officers. 561 U.S. at 507 n.10. Nor is that question presented here: Of the roughly 1900 "administrative law judges" across all federal agencies, OPM, Administrative Law Judges, https://www.opm.gov/services-for-agencies/administrative-law-judges/#url=ALJs-by-Agency,

only about 150 ALJs in 25 agencies apparently preside—as SEC ALJs do—over adversarial enforcement proceedings subject to Sections 556 and 557 of the APA. The vast majority of the remaining ALJs (more than 1650) administer Social Security benefits determinations in non-adversarial proceedings.

The only question in this case is whether the five SEC ALJs—who preside over adversarial enforcement proceedings—are Officers. As the applicable statutes confirm, *that* question must be answered in the affirmative. Adjudicators who wield such significant federal power in a manner that affects the liberty and property rights of citizens are precisely the sort of officials whose appointment should be "accountable to the political force and the will of the people." *Freytag*, 501 U.S. at 884. No "mere employee" can make evidentiary and legal determinations that so profoundly affect individual liberty as Judge Elliot did here.

* * *

The bottom line is that SEC ALJs are executive Officers, as the government now concedes. The remaining question is what this Court should do to redress the constitutional violation that Lucia has suffered at the hands of the Commission.

II. THE CONSTITUTIONAL VIOLATION REQUIRES A MEANINGFUL REMEDY

Because the D.C. Circuit erred in denying Lucia's petition for review, the judgment below should be reversed and the Commission's unlawful decision and order "set aside." 5 U.S.C. § 706(2). Among other things, that would free Lucia from the permanent bar imposed on him at the conclusion of the administrative proceeding (and which has not been stayed during the lengthy period of judicial review).

Because the underlying adjudication itself was conducted in violation of the Appointments Clause, the Constitution requires a new "hearing before a properly appointed" adjudicator. *Ryder*, 515 U.S. at 188; *see also United States* v. *L.A. Tucker Truck Lines, Inc.*, 344 U.S. 33, 38 (1952) (a "defect in [an] examiner's appointment ... would invalidate a resulting order" assuming a timely objection). At minimum, therefore, Lucia is entitled to an entirely new proceeding before a constitutional Officer. A recent order by the SEC, however, indicates that the more consequential remedy of dismissal is appropriate in this case.

A. An Entirely New Proceeding Is Necessary

Where, as here, the federal government has subjected a citizen to proceedings before an unconstitutionally appointed adjudicator, the Constitution requires entirely new proceedings before a constitutional Officer—for two reasons. First, because only a constitutional Officer can exercise significant authority of the United States, the actions of a non-Officer purporting to exercise such authority are null and void. Second, because the Appointments Clause protects inherently "structural interests," *Freytag*, 501 U.S. at 880, an Appointments Clause violation taints the entire proceeding. From a constitutional perspective, therefore, it is as if the proceedings before Judge Elliot never occurred, and the constitutional error can be remedied only by vacating everything done on Judge Elliot's watch.

1. This Court made clear in *Ryder* that, when a non-Officer presides over an adjudicatory proceeding, that proceeding is a nullity as a matter of constitutional law.

In *Ryder*, the government argued that the decisions of two civilian judges on the Court of Military Review who had not been constitutionally appointed were nevertheless valid under "[t]he *de facto* officer doctrine," which in some circumstances "confers validity upon" acts despite technical defects in the actor's title to office. 515 U.S. at 180. But the Court rejected the government's position, holding "that the judges' actions were not valid *de facto*," *id.* at 179, because—unlike other, technical defects to title—an Appointments Clause violation implicates deep separation-of-powers principles, *id.* at 182. The challenger thus was constitutionally entitled to "a hearing before a properly appointed panel." *Id.* at 188.

An entirely new proceeding is constitutionally required because the Appointments Clause serves no "frivolous purpose": It establishes the "exclusive method by which those charged with executing the laws of the United States may be chosen." *Buckley*, 424 U.S. at 118, 125; *see also id.* at 141 (significant authority may be "exercised *only* by persons who are 'Officers of the United States'" (emphasis added)). The Clause is such a critical safeguard that even a litigant's consent to the participation of an unconstitutionally appointed official does not preclude relief. *See Freytag*, 501 U.S. at 878-79.

This Court has been unwavering in recognizing that a defect in "the appointment" of the adjudicator "goes to the validity" of the underlying proceeding. *Freytag*, 501 U.S. at 879; *see also L.A. Tucker Truck Lines*, 344 U.S. at 38 (defect in the appointment of an Officer is "an irregularity" such that the "order should be set aside as a nullity"). Where, as here, the government has engaged in official action in derogation of the Appointments Clause, it is thus on notice that the

consequence of its constitutional violation is, at minimum, an entirely new proceeding.

"Any other rule," this Court has recognized, "would create a disincentive to raise Appointments Clause challenges." *Ryder*, 515 U.S. at 183. After all, without a new hearing, even *successful* challengers would realize no tangible benefit from "protecting the separation-of-powers interests at stake." *Freytag*, 501 U.S. at 879. Likewise, if there is no meaningful consequence for violating the Appointments Clause, the government would have no incentive to comply with its requirements. Because "[t]he structural interests protected by the Appointments Clause are not those of any one branch of Government," the legislative and executive branches cannot be relied upon to police each other in this area. *Id.* at 880.

2. An Appointments Clause violation also requires an entirely new proceeding because an improper adjudicator's participation "affect[s] the ... whole adjudicatory framework." *Williams* v. *Pennsylvania*, 136 S. Ct. 1899, 1910 (2016). Indeed, that is the very nature of a structural error: it undermines the proceedings so fundamentally that "the effects of the error are simply too hard to measure." *Weaver* v. *Massachusetts*, 137 S. Ct. 1899, 1908 (2017).

Where one judge on a multimember court sits in violation of the Constitution, for example, "it is neither possible nor productive to inquire whether the jurist in question might have influenced the views of his or her colleagues during the decisionmaking process." *Williams*, 136 S. Ct. at 1909. The complaining party must "be granted an opportunity to present his claims to a court unburdened" by the constitutional error—and only "rehearing" can provide that. *Id.* at 1910; *see also Nguyen* v. *United States*, 539 U.S. 69, 80-83

(2003) (participation of a statutorily ineligible panel member requires "fresh consideration ... by a properly constituted panel").

This principle admits of no shortcuts. A litigant who proves that the trial judge was biased, for example, does not win review by a disinterested judge to determine whether the decision was nevertheless fair—he "is entitled to a neutral and detached judge in the first instance." *Ward* v. *Vill. of Monroeville*, 409 U.S. 57, 61-62 (1972). A judge disqualified by a "direct pecuniary interest in the outcome" of the proceeding cannot cure the violation retroactively by forfeiting any monetary gain; "[n]o matter what the evidence [is] against" the defendant, he is "entitled to halt the trial" because "he ha[s] the right to have an impartial judge." *Tumey* v. *Ohio*, 273 U.S. 510, 535 (1927). And a litigant who proves racial discrimination in the selection of a grand jury is entitled to an entirely new trial, "even if [the] grand jury's determination of probable cause is confirmed in hindsight by a conviction on the indicted offense." *Vasquez* v. *Hillery*, 474 U.S. 254, 263 (1986).

3. The Appointments Clause violation here thus requires the Court to "set aside as a nullity" all of Judge Elliot's actions going back to the Commission's issuance of the order instituting proceedings, the last official act before the involvement of an unconstitutional adjudicator. *L.A. Tucker Truck Lines*, 344 U.S. at 38. There is no question but that Judge Elliot's participation "affected ... the whole adjudicatory framework below." *Williams*, 136 S. Ct. at 1910.

Judge Elliot received the parties' briefs; presided over an adversarial hearing; ruled on motions; admitted, excluded, and evaluated evidence; and issued two initial decisions, in which he made conclusions of law

and findings of fact. The Commission even remanded the case to him to make additional factual findings because its own "'review of the record [could] not replace [Judge Elliot's] personal experience with the witnesses.'" Pet. App. 241a (citation omitted). Because Judge Elliot was not entitled to exercise such authority, *all* of his actions are null and void. Anything less would deny Lucia "all the possibility for relief" from a constitutionally appointed Officer, *Ryder*, 515 U.S. at 187, because a different and neutral adjudicator could well have reached—or might in the future reach—a contrary conclusion as to both liability and sanctions than Judge Elliot did.

Just as an adjudicator disqualified by pecuniary interest could not retry a case after divesting himself of that interest, an ALJ who has held office in derogation of the Constitution cannot thereafter sit in judgment of the same proceeding, even if he later receives a proper appointment. Accordingly, Judge Elliot is disqualified from presiding over any remand proceedings involving Lucia. Indeed, it is doubtful whether *any* SEC ALJ could preside neutrally over such proceedings given Lucia's challenge to their authority to hold office. Due process requires "[a] fair trial in a fair tribunal," *In re Murchison*, 349 U.S. 133, 136 (1955), in "administrative agencies which adjudicate as well as [in] courts," *Withrow* v. *Larkin*, 421 U.S. 35, 46 (1975). The Commission could avoid these problems by bringing any remand action in an Article III court.

The Commission's review of Judge Elliot's initial decisions has no bearing on the remedy the Constitution itself requires for an Appointments Clause violation. Because Judge Elliot did not constitutionally hold office when he presided over the administrative

proceeding, there was (and is) *nothing* for the Commission to "review." The Commission could have presided over this administrative proceeding itself in the first instance, *see* 5 U.S.C. § 556(b)(1), 17 C.F.R. § 201.110, but having chosen to delegate the proceeding to an unconstitutional adjudicator, the Commission must accept the consequences of its own decision. That means that, at minimum, everything following the entry of the order instituting proceedings must be vacated, and the case remanded for an entirely new proceeding before a constitutional adjudicator.

Of course, the remedial order in this case could also have implications for other cases in which an Appointments Clause objection has been raised. To our knowledge there are only thirteen such cases pending in federal appellate courts on petitions for review of SEC enforcement actions:

- *SEC* v. *Bandimere*, No. 17-475 (S. Ct.);
- *Gonnella* v. *SEC*, No. 16-3433 (2d Cir.);
- *Bennett* v. *SEC*, No. 16-3827 (8th Cir.);
- *Aesoph* v. *SEC*, No. 16-3830 (8th Cir.);
- *Feathers* v. *SEC*, No. 15-70102 (9th Cir.);
- *Cooper* v. *SEC*, No. 15-73193 (9th Cir.);
- *J.S. Oliver Cap. Mgm't* v. *SEC*, No. 16-72703 (9th Cir.);
- *Malouf* v. *SEC*, No. 16-9546 (10th Cir.);
- *Timbervest, LLC* v. *SEC*, No. 15-1416 (D.C. Cir.);
- *Young* v. *SEC*, No. 16-1149 (D.C. Cir.);
- *Riad* v. *SEC*, No. 16-1275 (D.C. Cir.);

- *Robare Grp., Ltd.* v. *SEC*, No. 16-1453 (D.C. Cir.); and
- *Harding Advisory LLC* v. *SEC*, No. 17-1070 (D.C. Cir.).

The Commission has already asked the courts in most, if not all, of these cases to hold them in abeyance pending the Court's ruling in this case. *See, e.g.*, Order, *Timbervest, LLC* v. *SEC*, No. 15-1416 (D.C. Cir. Aug. 8, 2017). And the constitutional objections in those cases have already put the Commission "on notice of the accumulating risk of wholesale reversals being incurred by its persistence." *L.A. Tucker Truck Lines*, 344 U.S. at 37. If the Commission must start over in a baker's dozen other proceedings, the sky will not fall.

B. Dismissal Is Warranted

The remedy for a structural error must be "appropriate to the violation." *Waller* v. *Georgia*, 467 U.S. 39, 50 (1984). While ordinarily a new proceeding before a constitutional Officer could be an appropriate remedy for the Commission's longstanding failure to appoint its ALJs in a constitutional manner, an order recently entered by the Commission indicates that stronger medicine is needed in Lucia's case.

One day after the Solicitor General confessed error by acknowledging that SEC ALJs are Officers under the Appointments Clause, the Commission—which pointedly did not sign the Solicitor General's certiorari-stage brief—entered an order purporting to "put to rest" the constitutional issue. *See* Order, *In re Pending Administrative Proceedings*, Securities Act Release No. 10,440, at 1 (Nov. 30, 2017) ("Ratification Order"). The Commission ostensibly "ratifie[d] the agency's prior appointment" of its five ALJs, and di-

rected them to "[r]econsider the record" in open enforcement proceedings to determine "whether to ratify or revise in any respect *all prior actions taken*." *Id.* at 1-2 (emphasis added). While the order by its terms is limited to actions still pending before the agency (and thus does not moot this case), *see* Cert. Reply 5-9, it is an important preview of how the Commission intends to treat Lucia and other victims of the unconstitutional regime here challenged.

The so-called Ratification Order shows that the Commission still considers the Appointments Clause a mere "matter of 'etiquette or protocol.'" *Edmond*, 520 U.S. at 659 (citation omitted). The Commission accepts neither the Clause's command (since the SEC still has not properly appointed its ALJs) nor the consequences of violating that command (as the SEC refuses to provide the new hearings required by the Constitution). The Ratification Order also previews that, unless this Court directs otherwise, the Commission intends to simply return *this* case to Judge Elliot and instruct him to "ratify" his previous work (as Judge Elliot has done thus far in virtually every other case). That would literally add insult to injury, and necessitate another trip up the appellate ladder for Mr. Lucia—who has already been mired in these unconstitutional proceedings for too much of his life.

To send a clear message that the Constitution actually means what it says, the Court should instruct the Commission to dismiss the order instituting proceedings in this case. Otherwise, the Court "will have awarded petitioners a remarkably hollow victory." *Arthur Andersen LLP* v. *Carlisle*, 556 U.S. 624, 629 (2009).

1. To this day, there are no constitutionally appointed ALJs at the SEC. The Commission, as the

"Hea[d] of Departmen[t]" under the Appointments Clause, *could* appoint its ALJs. *See Free Enter. Fund*, 561 U.S. at 512-13 (quoting U.S. Const. art. II, § 2, cl. 2). An Officer's appointment requires a Commission vote, the administration of the oath of office, *see* U.S. Const. art. VI, cl. 3, and the signing and delivery of a commission, *see id.* art. II, § 3; *see also Marbury* v. *Madison*, 5 U.S. (1 Cranch) 137, 157 (1803) (delivery of commission is "evidence of an appointment"). These constitutional prescriptions are not mundane "wall ornament[s]"; rather, they ensure "accountability" by "identify[ing] the source" of an appointment and "confirm" that "[t]hose who exercise the power of Government are set apart from ordinary citizens. Because they exercise greater power, they are subject to special restraints." *Ass'n of Am. R.Rs.*, 135 S. Ct. at 1234-35 (Alito, J., concurring). Agencies, officials, and the public at large should know—and be able to ascertain—who are Officers.

To our knowledge, the Commission has done none of these things, other than (presumably) vote to "ratif[y] the agency's prior appointment." Ratification Order 1. That phrase, however, is constitutionally nonsensical. There was no "prior appointment" to ratify—the ALJs were not appointed by the agency, but rather were "hired" by the Chief ALJ, U.S. Cert. Br. 3. The Chief ALJ's previous "hiring" of ALJs was the constitutional equivalent of her "hiring" a new Chief Justice of the United States—that is to say, it was a nullity. Because that "hiring" did not satisfy the Appointments Clause, as the government now admits, the "ratification" of that same "hiring" cannot satisfy the Appointments Clause. The "ratification" of a nullity is itself a nullity.

This result follows directly from the "principles of agency law" that presumptively govern ratification. *FEC* v. *NRA Political Victory Fund*, 513 U.S. 88, 98 (1994). Ratification operates only to grant retroactive effect to an unauthorized act "as though authority to do the act *had been previously given*." *Cook* v. *Tullis*, 85 U.S. 332, 338 (1874) (emphasis added). Although a principal can ratify "a prior act ... which was done ... on his account" but without his authorization, Restatement (Second) of Agency § 82 (Am. Law Inst. 2017), a principal cannot ratify an act that would have been invalid even *with* his authorization, *see id.* § 86; *see also* 2A William M. Fletcher, *Encyclopedia of the Law of Corporations*, § 764 (2017) ("A void act cannot be validated by subsequent ratification"). Put differently, "[r]atification serves to authorize that which was unauthorized. Ratification cannot, however, give legal significance to an act which was a nullity from the start." *Newman* v. *Schiff*, 778 F.2d 460, 467 (8th Cir. 1985).

The Commission cannot retroactively "ratify" a hiring process that would have been invalid even if the Commission had originally authorized it. *See NRA Political Victory Fund*, 513 U.S. at 98-99. It is not as if the Chief ALJ could have "hired" or even "appointed" other ALJs, but simply lacked the Commission's say-so. *See, e.g.*, *Dep't Clerks-Delegation of Power*, 21 Op. Att'y Gen. 355, 356 (1896) ("The power to appoint ... can not be delegated"); *see also Freytag*, 501 U.S. at 878 (Clause adopted to prevent "diffusion of the appointment power"). Rather, because SEC ALJs are Officers, the Appointments Clause required *the Commission*, as "Hea[d] of Departmen[t]," to appoint them. U.S. Const. art. II, § 2, cl. 2. The government has admitted that never happened; therefore, as of today, there are *no* constitutionally appointed SEC

ALJs—and there will be none unless and until the Commission obeys the Constitution.

2. Even if the Commission were in the future to appoint its ALJs as required by the Constitution, it could not use "ratification" to salvage proceedings presided over by ALJs at a time they were not constitutionally appointed.

a. The Commission has forfeited any ability to invoke ratification in Lucia's particular case. As Lucia argued below, "the Enforcement Division did not argue before the Commission, and the Commission did not argue before the panel," or the en banc D.C. Circuit, "that the structural constitutional error in the improper appointment of its ALJ can be overlooked or excused under harmless-error, *ratification*, *de facto*-officer, or any similar doctrines." Lucia En Banc C.A.D.C. Br. 17 n.2 (emphasis added). The Commission did not contend otherwise in the court of appeals; on the contrary, the panel opinion expressly noted that "the government d[id] not argue harmless error would apply." Pet. App. 9a.

As Lucia explained in his petition (at 34), the Commission could not raise any ratification argument in this Court, *see SEC* v. *Chenery Corp.*, 318 U.S. 80, 87 (1943), and the government did not dispute that proposition at the certiorari stage. And because the Court-appointed *amicus* stands in the Commission's shoes, *see Greenlaw* v. *United States*, 554 U.S. 237, 250 & n.5 (2008), he may not raise any such argument either. Nor could the Commission use "ratification" to achieve the same result on any remand—the knowing forfeiture of that doctrine here precludes reliance on it in this case, even if, *dubitante*, it might be available in some other case.

b. More generally, "ratification" is unavailable in proceedings presided over by an unconstitutional official because parties to those proceedings are entitled to not only a *decision* from an Officer, but also *the process* of presenting their case from start to finish before an Officer. Plainly, "review" by a newly appointed Officer of actions already undertaken by that same official, or even another, does not give administrative respondents "all the possibility for relief" they would receive in an entirely new proceeding. *Ryder*, 515 U.S. at 187.

Persons accused of wrongdoing in SEC administrative proceedings are entitled to the procedural protections of sections 556 and 557 of the APA, including the presence of a lawfully appointed adjudicator at all stages of the proceeding. 5 U.S.C. § 556(b). If the Commission's human resources director or window washer oversaw an administrative proceeding, it would be absurd to suppose that an ALJ (or even the Commission itself) could pick up mid-stream, "ratify" the previous procedural and substantive choices made, and issue a valid decision on the merits. Yet that is essentially equivalent to the process contemplated by the Ratification Order.

The APA's requirements on this point reflect common-sense principles that apply equally outside the confines of administrative law. A judge who accepts a bribe to favor one party at trial cannot cure the violation by giving the money back and "ratifying" his decision. A verdict returned by an unsworn jury cannot be "ratified" after the fact by swearing in the jury and asking the foreperson to say "guilty" once more. And a judge who has occupied his seat and made myriad decisions absent the constitutionally prescribed mechanism for ensuring political accountability cannot,

once properly appointed, simply sign off on his old work. In all these cases, to permit 'ratification' would be to "confe[r] validity" upon the acts of an unconstitutional actor in violation of this Court's teachings. *Ryder*, 515 U.S. at 180.

The Commission's Ratification Order makes no attempt to square its commands with *Ryder*, *L.A. Tucker Truck Lines*, or any other of this Court's precedents concerning the consequences of an Appointments Clause violation. On the contrary, the Commission has told this Court and all the world how it plans to use the ratification doctrine to achieve, *mutatis mutandis*, precisely what this Court has already foreclosed under the *de facto* officer doctrine. *Ryder*, 515 U.S. at 179. This Court's precedents cannot be avoided so easily.

The Enforcement Division has thus far cited only one lower-court decision that even arguably suggests that an unconstitutional adjudicator's decision may be ratified. *See Intercollegiate Broad. Sys., Inc.* v. *Copyright Royalty Bd.*, 796 F.3d 111 (D.C. Cir. 2015). *Intercollegiate* is inapposite, as the Copyright Royalty Board does not adjudicate adversarial enforcement proceedings; the case is also both wrong and readily distinguishable.

In *Intercollegiate*, the D.C. Circuit held that review of the paper record assembled by an adjudicator serving in violation of the Appointments Clause can take the place of a new hearing, at least where "a properly appointed official has the power to conduct an independent evaluation of the merits and does so." 796 F.3d at 117. But the court did not even consider the established principle that the participation of an improper adjudicator renders the entire proceeding—

not just the ultimate decision—a nullity. *See Williams*, 136 S. Ct. at 1910; *see also L.A. Tucker Truck Lines*, 344 U.S. at 38. A *new* hearing is required because there *is* no record to "ratify"; whether the adjudicator was a window washer or an ALJ, the adjudicator's actions in shaping the record were a nullity. The D.C. Circuit's contrary conclusion is just plain wrong.

In any event, *Intercollegiate* is distinguishable because it held that the requirements for a new hearing on remand were "governed by ... the procedures set forth in the Copyright Act." 796 F.3d at 125. Whereas those requirements may permit "a papers-only proceeding," *id.* at 126; *see* 15 U.S.C. § 803(b)(5), the APA requires a constitutionally appointed officer "at the taking of evidence," 5 U.S.C. § 556(b). No "ratification" process can change that the adjudicator who "took" the evidence here was not, in fact, constitutionally appointed.

The Commission cannot sweep under the rug the constitutional violation that—the government now admits—occurred in this case. Whether the Commission calls it "ratification," or *de facto* officer, or harmless error, or anything else, the concept of "no harm, no foul" simply does not apply to such structural violations. Lucia was entitled to a proceeding before a constitutional Officer; and no such proceeding has been held in this case.

3. The Ratification Order makes clear that unless this Court imposes real, concrete consequences for the Commission's violations, the Commission does not intend to provide Lucia the constitutional minimum remedy to which he is entitled. The Court needs to make clear that the Commission cannot relegate a

"significant structural safeguar[d] of the constitutional scheme," *Edmond*, 520 U.S. at 659, to a mere footnote.

An appropriate response to the Commission's intransigence would be to order the Commission to dismiss the order instituting proceedings against Lucia. Lucia properly raised the Appointments Clause objection before the Commission; he has litigated it before a three-judge panel of the D.C. Circuit as well as the ten-judge en banc court; and he has now brought it to this Court for final disposition. At significant personal, financial, emotional, physical, and familial expense—and all the while subject to the Commission's bar order—Lucia has fought the good fight. *See generally* Ben Stein, *Now for a Few Words about the Rule of Law*, Am. Spectator (Feb. 13, 2018), http://bit.ly/2BqvklM. He should be rewarded with something more for his efforts than a decision in the U.S. Reports with his name on it.

The Court has already recognized that the remedy for an Appointments Clause violation should provide an appropriate incentive for litigants to maintain structural constitutional challenges, and disincentive for the government to resist them. *See Ryder*, 515 U.S. at 182-83, 186; *Freytag*, 501 U.S. at 879-80. In the context of this case, that means dismissal of the Commission's case against Lucia in its entirety. Dismissal would be especially appropriate here because there undisputedly were no investor losses, no misappropriated funds, and no customer complaints, *see* Pet. App. 101a, 129a, and thus letting Lucia have his life back would benefit him and his family to the detriment of no one.

* * *

The Commission's unconstitutional enforcement regime has inflicted devastating consequences on Ray Lucia. After an unblemished career spanning forty years, Mr. Lucia found himself in an SEC administrative proceeding with flimsy procedural protections and an adjudicator accountable to nobody. He now finds himself nearly bankrupt, exiled from his lifelong profession, legally precluded from working with his own son, and falsely branded a fraudster. His good name and reputation have already been tarnished by a federal official who had no constitutional authority to render such a life-altering decision. If the Commission has its way, these unconstitutional acts will dog Ray and his family indefinitely.

The Framers designed the Appointments Clause to prevent such abuses of power by unaccountable officials. This Court should make clear not only that the Appointments Clause was violated here, but that such a violation carries meaningful consequence.

CONCLUSION

The judgment of the court of appeals should be reversed and remanded with instructions to dismiss the order instituting proceedings or, in the alternative, for entirely new proceedings in a constitutional tribunal.

Respectfully submitted.

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No. 17-130

In the Supreme Court of the United States

RAYMOND J. LUCIA, ET AL., PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE RESPONDENT

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QUESTION PRESENTED

Whether the Securities and Exchange Commission's use of administrative law judges as hearing officers in administrative proceedings violates constitutional limitations on "Officers of the United States." U.S. Const. Art. II, § 2, Cl. 2.

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In the Supreme Court of the United States

No. 17-130

RAYMOND J. LUCIA, ET AL., PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 3a-36a) is reported at 832 F.3d 277. The order of the en banc court of appeals denying the petition for review by an equally divided court (Pet. App. 1a-2a) is reported at 868 F.3d 1021. The opinion and order of the Securities and Exchange Commission (Pet. App. 37a-109a) are reported at 112 SEC Docket 1754, and are available at 2015 WL 5172953.

JURISDICTION

The judgment of the court of appeals was entered on August 9, 2016. The court granted rehearing and entered a new judgment denying the petition for review on June 26, 2017 (Pet. App. 1a-2a). The petition for a writ of certiorari was filed on July 21, 2017. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Congress has created a comprehensive scheme for the commencement, adjudication, and judicial review of proceedings brought by the Securities and Exchange Commission (SEC or Commission) to enforce the Nation's securities laws. The Commission is authorized under the Securities Act of 1933, 15 U.S.C. 77a *et seq.*, the Securities Exchange Act of 1934, 15 U.S.C. 78a *et seq.*, the Investment Company Act of 1940, 15 U.S.C. 80a-1 *et seq.*, and the Investment Advisers Act of 1940, 15 U.S.C. 80b-1 *et seq.*, to address statutory violations by instituting administrative proceedings before the agency. See, *e.g.*, 15 U.S.C. 77h-1, 78u-3, 80a-9(b), 80a-41(a), 80b-3(e), (f), and (k); 15 U.S.C. 78d, 78*o* (2012 & Supp. IV 2016).

In an administrative enforcement proceeding, the Commission itself may preside and issue a final decision. 17 C.F.R. 201.110. In the alternative, Congress has authorized the Commission to delegate "its functions to a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee board." 15 U.S.C. 78d-1(a). Exercising this authority, the Commission has provided by rule that it may delegate the initial stages of conducting an enforcement proceeding to a "hearing officer." 17 C.F.R. 201.110. The hearing officer may be an administrative law judge (ALJ), a single Commissioner, multiple Commissioners (short of a quorum of the Commission), or "any other person duly authorized to preside at a hearing." 17 C.F.R. 201.101(a)(5).

The Commission historically has chosen to assign ALJs to act as hearing officers in its proceedings. Under 5 U.S.C. 3105, "[e]ach agency shall appoint as many

administrative law judges as are necessary for proceedings required to be conducted in accordance with sections 556 and 557 of this title," which are provisions governing agency hearings where an adjudication is required by statute to be determined on the record after an opportunity for a hearing. See 5 U.S.C. 553, 556, 557. The Commission currently employs five ALJs, who are hired through a competitive examination process conducted by the Office of Personnel Management (OPM). 5 U.S.C. 1104(a)(2); 5 C.F.R. 930.201.[1] OPM scores the examinations, ranks the candidates, and prepares a list of eligible candidates. See 5 C.F.R. 332.401, 332.402. In appointing ALJs, agencies may select from a top-three list of eligible candidates provided by OPM, 5 U.S.C. 3317(a), 3318(a), or they may select an ALJ who has an existing appointment from the same or a different agency, 5 C.F.R. 2.2(a). The Commission's ALJs are selected by its Chief ALJ, subject to approval by the Commission's Office of Human Resources on the exercise of authority delegated by the Commission. Pet. App. 295a-297a; cf. 15 U.S.C. 78d(b)(1) (Commission's authority to "appoint and compensate officers, attorneys, economists, examiners, and other employees").

In the capacity of a hearing officer in an SEC enforcement proceeding, an ALJ "shall have the authority to do all things necessary and appropriate to discharge his or her duties." 17 C.F.R. 201.111. Among other responsibilities, the ALJ may administer oaths; issue, revoke, quash, or modify subpoenas; receive and rule on the admission of evidence; withhold a party's access to agency documents; and "rul[e] upon all procedural and

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[1] See U.S. OPM, *ALJs by Agency* (Mar. 2017), https://www.opm.gov/services-for-agencies/administrative-law-judges/#url=ALJs-by-Agency.

other motions." 17 C.F.R. 201.111(h); see 17 C.F.R. 201.111(a), (b), and (c), 201.230(a)(1). In response to "[c]ontemptuous conduct" during a proceeding, the ALJ may exclude the contemnor from the hearing or may "[s]ummarily suspend that person from representing others in the proceeding." 17 C.F.R. 201.180(a)(1)(ii). If the ALJ concludes that a filed document "fails to comply" with the Commission's rules or with the ALJ's own orders, the ALJ may "reject" the filing, which "shall not be part of the record." 17 C.F.R. 201.180(b). The ALJ also may, under certain circumstances, deem a party to be "in default" and thus may "determine the proceeding against that party upon consideration of the record * * * , the allegations of which may be deemed to be true." 17 C.F.R. 201.155(a).

Following an administrative hearing, the ALJ must issue an "initial decision" within a specified number of days. 17 C.F.R. 201.360(a)(2). The ALJ's initial decision may be reviewed by the Commission *sua sponte* or at the request of a party or other aggrieved person. 17 C.F.R. 201.410, 201.411(c). If further review is not requested, or if the Commission declines to undertake such review, the ALJ's initial decision "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. 78d-1(c); see 17 C.F.R. 201.360(d)(2). When review by the Commission does occur, the Commission may "make any findings or conclusions that in its judgment are proper and on the basis of the record." 17 C.F.R. 201.411(a). The Commission also may remand the case to the ALJ to take additional evidence or may itself take additional evidence. 17 C.F.R. 201.452. The Commission will either issue its own opinion or will issue a "finality order"

stating that the ALJ's initial decision has become final and effective. 17 C.F.R. 201.360(d)(2); see Pet. App. 90a.

A party who is aggrieved by a final order of the Commission may seek judicial review of that order by filing a petition for review directly in a federal court of appeals. See 15 U.S.C. 77i(a), 78y(a)(1), 80a-42(a), 80b-13(a).

2. Petitioners were registered investment advisers who marketed a wealth-management strategy, which they called "Buckets of Money," under which retirement savings were divided among assets of different risk levels (*e.g.*, bonds, fixed annuities, and stocks) and periodically reallocated as those assets changed in value. Pet. App. 38a, 41a, 127a. The Commission instituted administrative proceedings against petitioners based on allegations that petitioners had used misleading slideshow presentations to deceive prospective clients about how the Buckets of Money strategy would have performed under historical market conditions. *Id.* at 41a-51a; see *id.* at 54a-62a (describing effects of alleged misrepresentations). The Commission charged petitioners with violating the Securities Exchange Act, the Investment Advisers Act, and the Investment Company Act. *Id.* at 238a.

a. The Commission assigned the initial stages of the proceeding to an ALJ, who conducted a hearing that lasted nine days. Pet. App. 116a. The ALJ presided over witness testimony and cross-examinations, admitted documentary evidence, and ruled on objections. Pet. 5. In so doing, the ALJ established "the official record" of the administrative proceeding. Pet. App. 117a n.2.

After the hearing, the ALJ issued an initial decision finding that petitioners had made fraudulent misrepresentations related to one of their investment strategies.

Pet. App. 117a. After the Commission directed the ALJ to make additional factual findings with respect to other alleged misrepresentations, *id.* at 118a, the ALJ issued a revised initial decision finding that respondents had willfully and materially misled investors, in violation of the Investment Advisers Act, *id.* at 195a-225a. The decision ordered a variety of sanctions to be imposed on petitioners, including revocation of their registrations as investment advisers; a permanent bar on associating with investment advisers, brokers, or dealers; a cease-and-desist injunction against future violations; and a total of $300,000 in civil monetary penalties. *Id.* at 235a; see *id.* at 225a-233a.

b. On appeal, the Commission conducted "an independent review of the record, except with respect to those findings not challenged on appeal." Pet. App. 40a. The Commission determined that the ALJ had correctly found that petitioners, in marketing their Buckets of Money Strategy, had willfully made fraudulent statements and omissions in violation of the Investment Advisers Act. *Id.* at 66a-86a. The Commission also largely "affirm[ed]," with limited exceptions, "the sanctions imposed below" by the ALJ. *Id.* at 95a; see *id.* at 95a-107a. Commissioners Gallagher and Piwowar dissented with respect to one aspect of the Commission's liability determination. *Id.* at 110a-114a.

Petitioners argued before the Commission that the proceedings against them were unlawful because the ALJ who had conducted the hearing and issued the initial decision was an "Officer[] of the United States" within the meaning of the Appointments Clause, U.S. Const. Art. II, § 2, Cl. 2. See Pet. App. 86a. Petitioners noted that the ALJ had not been appointed, in accordance with that provision, "by the President, the head of

a department, or a court of law." *Id.* at 87a. The Commission rejected petitioners' argument. In the Commission's view, its ALJs were mere employees rather than constitutional officers because they do not exercise "significant authority independent of the [Commission's] supervision." *Id.* at 88a. Among other things, the Commission explained, its ALJs "issue 'initial decisions' that are * * * not final," *id.* at 88a-89a; a person aggrieved by an initial decision may seek review before the Commission, which "grant[s] virtually all petitions for review," *id.* at 89a (citation omitted); the Commission may review any ALJ decision *sua sponte*, *ibid.*; review of an ALJ's decision is *de novo*, *id.* at 90a-91a; and under the Commission's rules, "no initial decision becomes final simply on the lapse of time by operation of law," but instead becomes final only upon "the Commission's issuance of a finality order," *id.* at 90a (citation and internal quotation marks omitted). The Commission also distinguished this Court's decision in *Freytag* v. *Commissioner*, 501 U.S. 868 (1991), in which special trial judges of the Tax Court were determined to be inferior officers under the Appointments Clause. Pet. App. 92a-93a; see *id.* at 92a ("*Freytag* [is] inapposite here.").

3. On appeal of the Commission's order, a panel of the court of appeals denied the petition for review. Pet. App. 3a-36a.

The court of appeals first rejected petitioners' Appointments Clause challenge, holding that the Commission's ALJs are mere employees rather than officers under the Clause because they do not exercise "significant authority pursuant to the laws of the United States." Pet. App. 11a (quoting *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam)); cf. *Buckley*, 424 U.S. at 126 n.162 (employees are "lesser functionaries subordinate

to officers"). For that conclusion, the court rested on its prior decision in *Landry* v. *FDIC*, 204 F.3d 1125, 1133-1134 (D.C. Cir.), cert. denied, 531 U.S. 924 (2000), holding that ALJs of the Federal Deposit Insurance Corporation (FDIC) did not exercise significant authority because they could not issue final decisions on behalf of the agency. Pet. App. 12a. The court determined that an SEC ALJ's initial decision is similarly non-final, and it rejected petitioners' attempts to distinguish *Landry*. *Id.* at 13a-19a; see *id.* at 15a ("Until the Commission determines not to order review * * * , there is no final decision that can 'be deemed the action of the Commission.'") (quoting 15 U.S.C. 78d-1(c)). The court also rejected petitioners' argument that the SEC's ALJs "exercise greater authority than FDIC ALJs in view of differences in the scope of review of the ALJ's decisions." *Id.* at 18a. The court acknowledged that "the Commission may sometimes defer to the credibility determinations of its ALJs," but it concluded that "the Commission's scope of review is no more deferential than that of the FDIC Board." *Id.* at 18a, 19a.

The court of appeals further rejected petitioners' attempt to equate the SEC's ALJs with the special trial judges of the Tax Court who were held to be officers in *Freytag*. In the court of appeals' view, the special trial judges were distinguishable because, as "members of an Article I court," they "could exercise the judicial power of the United States" and "issue final decisions in at least some cases." Pet. App. 11a, 12a. The court of appeals also found special trial judges to be different than SEC ALJs because "the Tax Court in *Freytag* was required to defer to the special trial judge's factual and credibility findings unless they were clearly erroneous."

Id. at 19a (citation and internal quotation marks omitted). The Commission, by contrast, "is not required to adopt the credibility determinations of an ALJ." *Ibid.*

On the merits, the court of appeals determined that substantial evidence supported the Commission's finding that petitioners, acting with the requisite scienter, had made material misstatements and omissions in violation of the Investment Advisers Act. Pet. App. 21a-32a. The court also concluded that the Commission had not abused its discretion in ordering sanctions against petitioners. *Id.* at 33a-36a.

4. Petitioners sought rehearing en banc, which the court of appeals granted on February 16, 2017. Pet. App. 244a-246a. The order granting rehearing en banc vacated the panel's judgment but not its opinion. *Id.* at 245a. The order directed the parties to limit their briefs to two issues: (1) whether "the SEC administrative law judge who handled this case [was] an inferior officer rather than an employee for the purposes of the Appointments Clause"; and (2) whether the court should "overrule *Landry*." *Ibid.* On June 26, 2017, the en banc court issued a per curiam judgment denying the petition for review "by an equally divided court." *Id.* at 1a-2a.

DISCUSSION

As this Court has previously observed, the question "[w]hether administrative law judges are necessarily 'Officers of the United States' is disputed." *Free Enterprise Fund* v. *Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 507 n.10 (2010) (quoting U.S. Const. Art. II, § 2, Cl. 2). In prior stages of this case, the government argued that the Commission's ALJs are mere employees rather than "Officers" within the meaning of the Appointments Clause. Upon further consideration, and in light of the implications for the exercise of executive

power under Article II, the government is now of the view that such ALJs are officers because they exercise "significant authority pursuant to the laws of the United States." *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam).

This Court's review is warranted. The courts of appeals are divided over whether the Commission's ALJs are officers. That division reflects pervasive uncertainty over the scope of this Court's holding in *Freytag* v. *Commissioner*, 501 U.S. 868 (1991), the only decision of this Court since *Buckley* to address the line between employees and officers under the Appointments Clause. The question presented has arisen frequently across the courts of appeals on petitions for review of the Commission's decisions, and it will continue to arise absent this Court's intervention. The question is also extremely important because it affects not merely the Commission's enforcement of the federal securities laws, but also the conduct of adversarial administrative proceedings in other agencies within the government. The petition for a writ of certiorari therefore should be granted, and this Court should appoint an amicus curiae to defend the judgment below.

A. The Commission's ALJs Are Officers Of The United States Rather Than Employees

1. The Constitution vests "[t]he executive Power" of the United States in the President, U.S. Const. Art. II, § 1, Cl. 1, who is charged with responsibility to "take Care that the Laws be faithfully executed," *id.* § 3. The Framers, however, recognized that, "in a republican government," the President would need to rely on the assistance of subordinate officials "to give dignity, strength, purity, and energy to the administration of

the laws." 3 Joseph Story, *Commentaries on the Constitution of the United States* § 1524, at 376 (1833). The Constitution accordingly authorizes the "establish[ment] by Law" of additional executive "Offices," and provides for them to be filled by "Officers of the United States." U.S. Const. Art. II, § 2, Cls. 1, 2; see William Rawle, *A View of the Constitution of the United States of America* 151, 152 (photo. reprint 2003) (2d ed. 1829) (describing the creation of "[s]ubordinate offices" as being "[a]mong the means provided to enable the president to perform his public duties").

The Appointments Clause sets out the exclusive method for appointment of all such Executive Branch officers whose appointments are not otherwise provided for in the Constitution. "[P]rincipal Officer[s]" are appointed by the President, by and with the advice and consent of the Senate; the same method applies to "inferior Officers," except where their appointments have instead been vested by law "in the President alone, in the Courts of Law, or in the Heads of Departments." U.S. Const. Art. II, § 2, Cls. 1, 2; see *United States* v. *Germaine*, 99 U.S. 508, 510 (1879) ("[A]ll persons who can be said to hold an office under the government about to be established under the Constitution were intended to be included within one or the other of these modes of appointment."). The requirements of the Appointments Clause are "among the significant structural safeguards of the constitutional scheme" and are "designed to preserve political accountability relative to important Government assignments." *Edmond* v. *United States*, 520 U.S. 651, 659, 663 (1997).

In *Buckley*, *supra*, the Court explained that "the term 'Officers of the United States' as used in Art. II"

includes all those who hold a position "under the government" and "exercis[e] significant authority pursuant to the laws of the United States." 424 U.S. at 125-126 (citations and internal quotation marks omitted). That description reflects the common understanding at the time of the Founding that "[a] public office is the right, authority and duty, created and conferred by law, by which for a given period * * * an individual is invested with some portion of the sovereign functions of government, to be exercised by him for the benefit of the public." Floyd R. Mechem, *A Treatise on the Law of Public Offices and Officers* § 1, at 1-2 (1890) (summarizing English and early American sources); see 2 Giles Jacob, *The Law-Dictionary*, Tit. "Office" (1797) ("[I]t is a rule, that where one man hath to do with another's affairs against his will, and without his leave, that this is an Office, and he who is in it is an officer."); see also 20 Op. O.L.C. 124, 178-187 (1996).[2]

2. Since *Buckley*, this Court has only once addressed the line between constitutional officers and

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[2] Early decisions of this Court addressing the Appointments Clause were primarily concerned with the question whether Congress *intended* to treat a position it had created by statute as an "office," not whether the functions of the position were required to be performed by an officer appointed pursuant to the Appointments Clause. See, *e.g.*, *Germaine*, 99 U.S. at 509 (civil surgeon could not be prosecuted under criminal statute applicable only to an "officer of the United States who is guilty of extortion") (citation omitted); *United States* v. *Hartwell*, 73 U.S. (6 Wall.) 385, 391-392 (1867) (statute forbidding embezzlement by "officers" applied to clerk appointed by the assistant treasurer in Boston with the approbation of the Acting Secretary of the Treasury) (discussed in *Germaine*, 99 U.S. at 511). In those cases, the Court looked at whether the appointment had occurred in the manner contemplated by the Clause as evidence for whether Congress intended to treat the appointee as an officer.

mere employees. In *Freytag*, *supra*, the Court considered whether certain Tax Court proceedings could be assigned, "for [a] hearing and the preparation of proposed findings and written opinion," to a special trial judge appointed by the Chief Judge of the Tax Court. 501 U.S. at 877. The petitioners in *Freytag* were taxpayers who had objected to tax deficiencies assessed against them and sought review in the Tax Court. *Id.* at 870-871. The proceedings were initially assigned to a special trial judge, who issued "written findings and an opinion" concluding that the petitioners owed additional taxes. *Id.* at 871-872. After unsuccessfully appealing that ruling to the Chief Judge, the petitioners "contended that the assignment of cases as complex as theirs to a special trial judge * * * violated the Appointments Clause of the Constitution." *Id.* at 872.

In addressing that claim, this Court at the outset considered whether "special trial judges may be deemed employees * * * because they lack authority to enter a final decision." *Freytag*, 501 U.S. at 881. That argument, the Court explained, "ignores the significance of the duties and discretion that special trial judges possess." *Ibid.* Unlike special masters, who are hired "on a temporary, episodic basis" to perform ad hoc tasks, special trial judges occupy an office "'established by Law,'" and the "duties, salary, and means of appointment for that office are specified by statute." *Ibid.* (quoting U.S. Const. Art. II, § 2, Cl. 2). The Court placed particular emphasis on the fact that special trial judges, in presiding over preliminary proceedings, "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders." *Id.* at 881-882. "In the course of car-

rying out these important functions," the Court explained, "special trial judges exercise significant discretion." *Id.* at 882.

The Court went on to hold that special trial judges would qualify as constitutional officers "[e]ven if" their ability to issue initial decisions in cases like petitioners' were not so "significant." *Freytag*, 501 U.S. at 882; *ibid.* ("[O]ur conclusion would be unchanged."). That is because, the Court explained, special trial judges are also authorized by law to "render the decisions of the Tax Court [*i.e.*, final decisions] in declaratory judgment proceedings and limited-amount tax cases." *Ibid.* Since it was not disputed that "a special trial judge is an inferior officer for purposes of" those proceedings, the Court concluded, their appointments must comply with the Appointments Clause for all purposes. *Ibid.* ("Special trial judges are not inferior officers for purposes of some of their duties * * * but mere employees with respect to other responsibilities."). Finally, having determined that the Appointments Clause applied to special trial judges, the Court held that their selection could properly be vested under that Clause in the Chief Judge of the Tax Court. *Id.* at 882-892.

Freytag demonstrates that the Commission's ALJs are "inferior officers" rather than "mere employees." 501 U.S. at 882. Like the special trial judges at issue there, the office of an SEC ALJ is characterized by significant "duties and discretion." *Id.* at 881. The position and its compensation have been established by law, see 5 U.S.C. 3105 (appointment authority), 5372(b) (compensation), and the Commission's ALJs have been entrusted with governmental authority "delegate[d]" from the Commission itself, 15 U.S.C. 78d-1(a). ALJs are authorized, among other things, to administer

oaths, hold hearings, take testimony and admit evidence, issue or quash subpoenas, rule on motions, impose sanctions on contemptuous hearing participants, reject deficient filings, and enter default judgments. See 17 C.F.R. 201.111(a), (b), (c), and (h), 201.180(a) and (b).[3] At the conclusion of a hearing, the ALJ issues an "initial decision" that "include[s] findings and conclusions * * * as to all the material issues of fact, law or discretion presented on the record and the appropriate order, sanction, relief, or denial thereof." 17 C.F.R. 201.360(b). If further review of the ALJ's decision is not sought, or a request for such review is denied by the Commission, the ALJ's initial decision "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. 78d-1(c); see 17 C.F.R. 201.360(d)(2). In discharging these responsibilities, an ALJ "exercise[s] significant discretion." *Freytag*, 501 U.S. at 881-882. The ALJ is thus an "Officer[ ]" within the meaning of the Appointments Clause.

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[3] The special trial judges at issue in *Freytag* were authorized to "punish contempts by fine or imprisonment." 501 U.S. at 891 (citing 26 U.S.C. 7456(c)). The Commission's ALJs, by contrast, have the arguably less significant authority to punish "[c]ontemptuous conduct" either by "[e]xclud[ing]" the contemnor from the deposition or hearing or by "[s]ummarily suspend[ing] that person from representing others in the proceeding." 17 C.F.R. 201.180(a)(1). The Court's decision in *Freytag*, however, did not identify the power to fine or imprison as evidence of "the significance of the duties and discretion that special trial judges possess." 501 U.S. at 881. Rather, the contempt power was cited only as support for the Court's conclusion that the Tax Court was a "'Court of Law' within the meaning of the Appointments Clause." *Id.* at 890 (brackets omitted); see *id.* at 890-891.

3. In ruling that the Commission's ALJs are not officers, the court of appeals gave dispositive weight to its perception that those ALJs have no authority to issue final decisions that "bind third parties, or the government itself, for the public benefit." Pet. App. 12a-13a; see *id.* at 13a ("Our analysis begins, and ends, there."). The court relied for that conclusion on its prior decision in *Landry* v. *FDIC*, 204 F.3d 1125 (D.C. Cir.), cert. denied, 531 U.S. 924 (2000), where the court read *Freytag* as treating final decision-making authority as the *sine qua non* of officer status. Pet. App. 11a-13a; see *id.* at 12a ("This court understood that it 'was critical to the Court's decision' in *Freytag* that the special trial judge had authority to issue final decisions in at least some cases.") (quoting *Landry*, 204 F.3d at 1134). The Commission's ALJs, the court of appeals asserted, cannot issue final decisions: An ALJ's initial decision "becomes final when, and only when, the Commission issues [a] finality order, and not before then." *Id.* at 15a; see *ibid.* ("[T]he Commission has retained full decision-making powers, and the mere passage of time is not enough to establish finality."). As a result, the court concluded, the "initial decisions are no more final than the recommended decisions issued by FDIC ALJs" that the court had upheld in *Landry*. *Id.* at 17a.

As petitioners here explain (Pet. 20-22), however, the court of appeals erred in placing conclusive weight on the lack of final decision-making authority by the Commission's ALJs. Although *Landry* treated that factor as "critical," 204 F.3d at 1134, *Freytag* held that special trial judges—in light of "the significance of the duties and discretion that [they] possess"—are properly considered officers under the Appointments Clause *despite*

their "lack [of] authority to enter a final decision" regarding tax-deficiency claims. 501 U.S. at 881. To be sure, the Court went on to say that special trial judges would be officers "[e]ven if" their authority over such cases were less "significant," given their authority to render final decisions in other types of cases. *Id.* at 882. But "the Court clearly designated [that statement] as an alternative holding." *Landry*, 204 F.3d at 1142 (Randolph, J., concurring in part and concurring in the judgment). The Court in *Freytag* thus indicated that final authority to make certain discretionary decisions may be sufficient, but is not necessary, to render an official an "Officer[] of the United States" within the meaning of the Appointments Clause.

In attempting to distinguish *Freytag*, the court of appeals further emphasized the relatively low level of deference afforded by the Commission to ALJ decisions. The Commission "reviews an ALJ's decision *de novo* and 'may affirm, reverse, modify, or set aside' the initial decision, 'in whole or in part,' and it 'may make any findings or conclusions that in its judgment are proper and on the basis of the record.'" Pet. App. 18a-19a (quoting 17 C.F.R. 201.411(a)) (brackets omitted). And while the Commission has chosen, as a matter of practice, to "defer to credibility determinations where the record provides no basis for disturbing the finding," the Commission is "not required to adopt the credibility determinations of an ALJ." *Id.* at 19a. By contrast, the court of appeals emphasized, "the Tax Court in *Freytag* was required to defer to the special trial judge's factual and credibility findings unless they were clearly erroneous." *Ibid.* (citation and internal quotation marks omitted).

The court of appeals' proposed distinction from *Freytag* is not persuasive. The level of deference afforded to the decisions of special trial judges played no role in the Court's conclusion that they qualified as "Officers" within the meaning of the Appointments Clause. See 501 U.S. at 880-882. The Court mentioned deference in a different portion of *Freytag* addressing the petitioners' statutory-construction argument, and even there the Court stated that the "point [wa]s not relevant." *Id.* at 874 n.3. Nor, in this case, does the Commission's relative lack of deference to the decisions of its ALJs call into question that such ALJs are "Officers of the United States" under the Appointments Clause. Finally, there is no merit to the court of appeals' attempt to distinguish *Freytag* on the ground that special trial judges were "members of an Article I court [who] could exercise the judicial power of the United States." Pet. App. 11a. In determining that the special trial judges were officers, *Freytag* did not even mention their status as judicial officials.

B. The ALJs' Status As Officers Has Implications For Both Their Selection And Removal That The Court Should Address

The conclusion that ALJs are "Officers of the United States" has important implications under the Constitution regarding the permissible method of their appointment and the manner in which they may be removed from office. This Court's guidance on both issues is accordingly necessary to enable the United States to assess the status of ALJs in various roles across the government and to consider whether the rules governing the selection and removal of those officials comport with constitutional requirements.

1. Under the Appointments Clause, Congress may "vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments." U.S. Const. Art. II, § 2, Cl. 2. The appointment of the ALJ who presided in petitioners' case did not conform to that command. That ALJ was selected by the Commission's Chief ALJ, subject to approval by the Commission's Office of Human Resources. See pp. 2-3, *supra*. The Commission itself, as the constitutional "Head[] of Department[]," did not play any role in the selection. See Pet. App. 295a-297a.

2. Because "Article II confers on the President 'the general administrative control of those executing the laws,' * * * the President therefore must have some 'power of removing those for whom he can not continue to be responsible.'" *Free Enterprise Fund*, 561 U.S. at 492-493 (quoting *Myers* v. *United States*, 272 U.S. 52, 117, 164 (1926)). This Court has accordingly recognized that the Constitution forbids Congress from placing certain restrictions on the power to remove officers of the United States. In *Free Enterprise Fund*, the Court invalidated a statutory scheme that provided for two levels of protection against presidential removal authority: Members of the Public Company Accounting Oversight Board (PCAOB) could be removed by the SEC only for certain limited forms of wrongdoing, see 15 U.S.C. 7217(d)(3), and the Court assumed that the SEC's Commissioners could themselves be removed only for "inefficiency, neglect of duty, or malfeasance in office," 561 U.S. at 487 (citation omitted). The Court determined that the combined effect of those restrictions, which resulted in the PCAOB's exercise of executive authority without any meaningful presidential oversight,

had caused a constitutionally impermissible "diffusion of accountability." *Id.* at 497; see *id.* at 495-508.

Here, the statutory scheme provides for at least two, and potentially three, levels of protection against presidential removal authority: The Commission's ALJs may be removed by the Commission "only for good cause established and determined by the Merit Systems Protection Board," 5 U.S.C. 7521(a), and members of that Board in turn "may be removed by the President only for inefficiency, neglect of duty, or malfeasance in office," 5 U.S.C. 1202(d). And the Commissioners likewise may be insulated from removal (as the Court assumed in *Free Enterprise Fund*), although the Securities Exchange Act is silent on the question. 15 U.S.C. 78d(a). Under *Free Enterprise Fund* and other decisions, the status of the Commission's ALJs as constitutional "Officers" therefore has implications for whether the statutory restrictions on their removal are consistent with separation-of-powers principles.

Petitioners assert (Pet. 34) that the issue of removal authority should be of no immediate concern to the Court because they have not directly challenged the removal restrictions on the ALJ who presided at their hearing. But petitioners do not dispute that the question whether the Commission's ALJs are impermissibly insulated from presidential oversight is informed by the conclusion that such ALJs are constitutional officers who exercise significant authority. See *Free Enterprise Fund*, 561 U.S. at 507 n.10 (reserving the question, in part, because "[w]hether administrative law judges are necessarily 'Officers of the United States' is disputed") (citing *Landry*, *supra*). And even if petitioners are successful in obtaining invalidation of the proceedings against them in this case, and further proceedings occur

in front of a properly appointed ALJ, the removal question would continue to cloud the ALJ's authority. Indeed, another litigant has already raised a separation-of-powers challenge to ALJ removal protections alongside an Appointments Clause challenge; that case has been briefed in the D.C. Circuit and is being held pending the disposition of this petition. See 8/8/17 Order, *Timbervest* v. *SEC*, No. 15-1416.

It is critically important that the Court, in considering whether the Commission's ALJs are "Officers of the United States," address whether the restrictions imposed by statute on their removal are consistent with the constitutionally prescribed separation of powers. Addressing that issue now will avoid needlessly prolonging the period of uncertainty and turmoil caused by litigation of these issues. See pp. 24-26, *infra*. If the Court believes that petitioners' framing of the question presented is not broad enough to encompass the issue, the government has reframed the question to leave no doubt on that score. In the alternative, the Court may find it desirable to add a question presented that specifically addresses it. See, *e.g.*, *NLRB* v. *Noel Canning*, 133 S. Ct. 2861 (2013) (directing the parties to brief and argue an additional question, which had not been considered by the courts below). Whatever the appropriate course, the government respectfully submits that addressing both the appointment and removal of the Commission's ALJs will provide needed clarity to agencies and regulated parties, while minimizing what could otherwise be severe disruption to a large number of current and future administrative proceedings.

C. This Case Is The Preferable Vehicle For Resolving The Division Among The Courts Of Appeals

This Court's review is warranted because the question presented has led to significant disagreement in the courts of appeals. That disagreement has generated substantial confusion and disruption for the Commission in its enforcement of the Nation's securities laws, as well as for other federal agencies that use ALJs in administrative proceedings.

1. In the proceeding below, a panel of the D.C. Circuit held that the Commission's ALJs are employees rather than officers. The court subsequently granted rehearing en banc, Pet. App. 244a-246a, and ultimately denied the petition for review by an equally divided vote, *id.* at 1a-2a. Under D.C. Circuit Rule 35(d), an order granting en banc review vacates "the panel's judgment, but ordinarily not its opinion." Consistent with that rule, the court's order granting rehearing en banc vacated only the panel's "judgment," 2/16/17 Order 1, leaving the panel's opinion undisturbed.

The Commission has therefore explained, in other cases raising Appointments Clause challenges, that the panel's opinion in this case remains in effect. See, *e.g.*, Commission Br. at 62, *Gonnella* v. *SEC*, No. 16-3433 (2d Cir. July 17, 2017). The Commission has also urged the D.C. Circuit to hold follow-on cases raising the same question in abeyance pending this Court's disposition of the petition for a writ of certiorari. See, *e.g.*, Mot. to Hold Case in Abeyance, *Timbervest, LLC* v. *SEC*, No. 15-1416 (July 20, 2017). The D.C. Circuit has granted those abeyance motions. See, *e.g.*, 8/8/17 Order, *Timbervest, LLC* v. *SEC*, No. 15-1416.

2. In *Bandimere* v. *SEC*, 844 F.3d 1168 (2016), a divided panel of the Tenth Circuit reached the opposite

conclusion on the question presented under materially identical circumstances. There, an ALJ issued an initial decision finding that the respondent had violated anti-fraud and registration provisions of the federal securities laws by operating as an unregistered broker and by failing to disclose potentially negative facts to investors. *In re David F. Bandimere*, Securities Act Release No. 9972, 2015 WL 6575665, at *1 (Oct. 29, 2015). On review of the ALJ's initial decision, the Commission upheld the liability finding and imposed disgorgement and civil-penalty sanctions. *Id.* at *2. The Commission also rejected the respondent's argument that its ALJs are officers under the Appointments Clause. *Id.* at *19-*21.

The Tenth Circuit granted the respondent's petition for review, holding that the Commission's ALJs are invested with powers that require their appointment as inferior officers under the Appointments Clause. *Bandimere*, 844 F.3d at 1179-1182. In reaching that conclusion, the court relied on *Freytag*, which it interpreted as turning on the significance of the special trial judges' duties, not on their authority to render final decisions of the Tax Court. *Id.* at 1182-1185; see *id.* at 1179 (The Commission's ALJs "exercise significant discretion in performing 'important functions' commensurate with the [special trial judges'] functions described in *Freytag*.") (quoting 501 U.S. at 882). The court thus expressly "disagree[d]" with the D.C. Circuit's decisions in *Landry* and in this case, which, the Tenth Circuit determined, had "place[d] undue weight on final decision-making authority." *Id.* at 1182.

Judge McKay dissented, arguing that *Freytag* does not "mandate[] the result proposed here." *Bandimere*, 844 F.3d at 1194. Like the panel in this case, Judge

McKay distinguished the special trial judges at issue in *Freytag* because of their authority to enter final decisions in a number of cases and because "the Tax Court was required to defer to its special trial judges' findings." *Id.* at 1197. Judge McKay emphasized that the Commission's ALJs, by contrast, "possess only a 'purely recommendatory power.'" *Ibid.* (quoting *Landry*, 204 F.3d at 1132). In May 2017, the Tenth Circuit denied the Commission's petition for rehearing en banc, with Judges Lucero and Moritz dissenting. See *Bandimere* v. *SEC*, 855 F.3d 1128, 1128-1133.

On September 29, 2017, the government filed a petition for a writ of certiorari in *SEC* v. *Bandimere*, No. 17-475, urging this Court to resolve the question whether the Commission's ALJs are inferior officers rather than employees. But the government explained that this case, rather than *Bandimere*, presents the Court with the preferable vehicle for addressing that question. See Pet. at 9, *Bandimere*, *supra* (No. 17-475). The government accordingly "respectfully request[ed] that the Court hold th[e] petition" in *Bandimere* "pending its consideration of the petition" in this case. *Ibid.*

3. The disagreement in the courts of appeals has significant implications for the Commission's ability to discharge its statutory responsibilities. Congress has granted the Commission broad authority to conduct administrative enforcement proceedings to determine whether the securities laws have been violated and, if so, what remedies are appropriate. See 15 U.S.C. 77h-1, 78u-3; 15 U.S.C. 78d, 78*o* (2012 & Supp. IV 2016). Certain of the Commission's enforcement powers, such as the power to revoke the registration of a registered security under 15 U.S.C. 78*l*(j), can be exercised *only* through the initiation of an administrative proceeding.

In conducting such proceedings, the Commission historically has assigned an ALJ to preside over the hearing and issue an initial decision, which the Commission then reviews. See 15 U.S.C. 78d-1(a). The abeyance status of cases pending in the D.C. Circuit—which has automatic venue in securities cases, see 15 U.S.C. 77i(a), 78y(a)(1), 80a-42(a), 80b-13(a)—thus means that the Commission's ability to enforce the nation's securities laws has, in significant respects, been put on hold pending this Court's resolution of the question presented. Appointments Clause challenges to the Commission's ALJs have also been raised in several other cases across the courts of appeals, indicating that the gridlock will soon be even more widespread.[4]

4. Finally, the conflict in the courts of appeals on the question presented has created substantial uncertainty for other agencies that employ ALJs in a manner similar to the Commission. A panel of the Fifth Circuit recently granted a stay of an FDIC order, concluding that the respondent had established a likelihood of success on his claim that the ALJ who presided over his proceeding was an officer who was not properly appointed under the Appointments Clause. *Burgess* v. *FDIC*, 871 F.3d 297 (2017). In so ruling, the court expressly disagreed with the D.C. Circuit's decision in *Landry*. *Id.* at 301 ("We therefore conclude, contrary to the D.C. Circuit's decision in *Landry*, that final decision-making authority is not a necessary condition for Officer sta-

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[4] See, *e.g.*, *Gonnella* v. *SEC*, No. 16-3433 (2d Cir. filed Oct. 7, 2016); *Bennett* v. *SEC*, No. 16-3827 (8th Cir. argued June 7, 2017); *J.S. Oliver Capital Mgmt., L.P.* v. *SEC*, No. 16-72703 (9th Cir. filed Aug. 15, 2016); *Feathers* v. *SEC*, No. 15-70102 (9th Cir. filed Jan. 9, 2015).

tus."). Given the frequency with which ALJs are employed in administrative proceedings by a variety of federal agencies, see, *e.g.*, 7 C.F.R. 1.144, 1.411(f) (Department of Agriculture); 12 C.F.R. 1081.103 (Consumer Financial Protection Bureau); 18 C.F.R. 385.102(e), 385.708 (Federal Energy Regulatory Commission); 29 C.F.R. 102.35 (National Labor Relations Board); 40 C.F.R. 22.3(a), 22.4(c) (Environmental Protection Agency), this Court's resolution of the question presented is necessary to prevent the same disruption that has affected the Commission's proceedings from spreading throughout the government.

CONCLUSION

The petition for a writ of certiorari should be granted. If appropriate, the Court should reframe the question presented or add a question presented to address the issue of removal.

Respectfully submitted.

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No. 17-130

In the Supreme Court of the United States

RAYMOND J. LUCIA, ET AL., PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR RESPONDENT SUPPORTING PETITIONERS

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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In the Supreme Court of the United States

No. 17-130

RAYMOND J. LUCIA, ET AL., PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR RESPONDENT SUPPORTING PETITIONERS

OPINIONS BELOW

The order of the en banc court of appeals denying the petition for review by an equally divided court (Pet. App. 1a-2a) is reported at 868 F.3d 1021. An opinion of the court of appeals (Pet. App. 3a-36a) is reported at 832 F.3d 277. The opinion and order of the Securities and Exchange Commission (Pet. App. 37a-109a) are reported at 112 SEC Docket 1754, and are available at 2015 WL 5172953.

JURISDICTION

The judgment of the court of appeals was entered on August 9, 2016. The court granted rehearing and entered a new judgment denying the petition for review on June 26, 2017 (Pet. App. 1a-2a). The petition for a writ of certiorari was filed on July 21, 2017. The petition was granted on January 12, 2018. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

CONSTITUTIONAL, STATUTORY, AND REGULATORY PROVISIONS INVOLVED

Pertinent constitutional, statutory, and regulatory provisions are reprinted in the appendix to this brief. App., *infra*, 1a-21a.

STATEMENT

1. Congress has created a comprehensive scheme for the commencement, adjudication, and judicial review of proceedings brought by the Securities and Exchange Commission (SEC or Commission) to enforce the Nation's securities laws. The Commission is authorized under the Securities Act of 1933, 15 U.S.C. 77a *et seq.*, the Securities Exchange Act of 1934, 15 U.S.C. 78a *et seq.*, the Investment Company Act of 1940, 15 U.S.C. 80a-1 *et seq.*, and the Investment Advisers Act of 1940, 15 U.S.C. 80b-1 *et seq.*, to address statutory violations by instituting administrative proceedings before the agency. See, *e.g.*, 15 U.S.C. 77h-1, 78u-3, 80a-9(b), 80a-41(a), 80b-3(e), (f), and (k); 15 U.S.C. 78d, 78*o* (2012 & Supp. IV 2016).

In an administrative enforcement proceeding, the Commission itself may preside and issue a final decision. 17 C.F.R. 201.110. In the alternative, Congress has authorized the Commission to delegate "its functions to a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee board." 15 U.S.C. 78d-1(a); see 5 U.S.C. 556(b) (in certain agency hearings, "the agency," "members of the body which comprises the agency," or "administrative law judges" may preside). Exercising that authority, the Commission has provided by rule that it may delegate the initial stages of conducting an enforcement proceeding to a "hearing officer." 17 C.F.R. 201.110. The hearing officer may be

an administrative law judge (ALJ), a single Commissioner, multiple Commissioners (short of a quorum of the Commission), or "any other person duly authorized to preside at a hearing." 17 C.F.R. 201.101(a)(5).

The Commission historically has chosen to assign ALJs to act as hearing officers in its proceedings. Under 5 U.S.C. 3105, "[e]ach agency shall appoint as many administrative law judges as are necessary for proceedings required to be conducted in accordance with sections 556 and 557 of this title," which are provisions governing agency hearings where a rulemaking or adjudication is required by statute to be determined on the record after an opportunity for a hearing. See 5 U.S.C. 553(c), 554(a), 556, 557. The Commission currently employs five ALJs,[1] who were selected by its Chief ALJ, subject to approval by the Commission's Office of Human Resources on the exercise of authority delegated by the Commission. Pet. App. 295a-297a.[2]

In the capacity of a hearing officer in an SEC enforcement proceeding, an ALJ "shall have the authority to do all things necessary and appropriate to discharge his or her duties." 17 C.F.R. 201.111. Among other responsibilities, the ALJ may administer oaths; issue, revoke, quash, or modify subpoenas; receive and rule on

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[1] See U.S. Office of Pers. Mgmt., *ALJs by Agency* (Mar. 2017), https://www.opm.gov/services-for-agencies/administrative-law-judges/#url=ALJs-by-Agency.

[2] The day after filing its response to the petition for certiorari in this case, the Commission ratified the appointment of its ALJs. See U.S. SEC, *Order* (Nov. 30, 2017), https://www.sec.gov/litigation/opinions/2017/33-10440.pdf. The Commission did not take any action, however, that would disturb cases, such as this one, that were already under judicial review at the time. See 15 U.S.C. 78y(a)(3) (court of appeals' jurisdiction over a case arising from the Commission becomes "exclusive on the filing of the record").

the admission of evidence; withhold a party's access to agency documents; and "rul[e] upon all procedural and other motions." 17 C.F.R. 201.111(h); see 17 C.F.R. 201.111(a), (b), and (c), 201.230(a)(1). In response to "[c]ontemptuous conduct" during a proceeding, the ALJ may exclude the contemnor from the hearing or may "[s]ummarily suspend that person from representing others in the proceeding." 17 C.F.R. 201.180(a)(1)(ii). If the ALJ concludes that a filed document "fails to comply" with the Commission's rules or with the ALJ's own orders, the ALJ may "reject" the filing, which "shall not be part of the record." 17 C.F.R. 201.180(b). The ALJ also may, under certain circumstances, deem a party to be "in default" and thus may "determine the proceeding against that party upon consideration of the record * * * , the allegations of which may be deemed to be true." 17 C.F.R. 201.155(a).

Following an administrative hearing, the ALJ must issue an "initial decision" within a specified number of days. 17 C.F.R. 201.360(a)(2). The ALJ's initial decision may be reviewed by the Commission *sua sponte* or at the request of a party or other aggrieved person. 17 C.F.R. 201.410, 201.411(c). If further review is not requested, or if the Commission declines to undertake such review, the ALJ's initial decision "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. 78d-1(c); see 17 C.F.R. 201.360(d)(2). When review by the Commission does occur, the Commission may "make any findings or conclusions that in its judgment are proper and on the basis of the record." 17 C.F.R. 201.411(a). The Commission also may remand the case to the ALJ to take additional evidence or may itself take additional

evidence. 17 C.F.R. 201.452. The Commission will either issue its own opinion or will issue an "order of finality" stating that the ALJ's initial decision has become final and effective. 17 C.F.R. 201.360(d)(2); see Pet. App. 90a.

A party who is aggrieved by a final order of the Commission may seek judicial review of that order by filing a petition for review directly in a federal court of appeals. See 15 U.S.C. 77i(a), 78y(a)(1), 80a-42(a), 80b-13(a).

2. Once appointed, the Commission's ALJs (like all ALJs) may be removed from their positions "only for good cause established and determined by the Merit Systems Protection Board [MSPB or Board] on the record after opportunity for hearing before the Board." 5 U.S.C. 7521(a); see 5 U.S.C. 7521(b)(1). Congress has not defined what constitutes "good cause" sufficient under Section 7521 to provide a basis for removing an ALJ. See pp. 48-49, *infra*. The Board is composed of three members who are appointed by the President with the Senate's consent, 5 U.S.C. 1201, and are removable by the President "only for inefficiency, neglect of duty, or malfeasance in office." 5 U.S.C. 1202(d).

Under regulations adopted by the Board, the employing agency, upon determining that an ALJ should be removed, submits a complaint to the Board detailing the relevant charges of misconduct or other cause for discipline. See 5 C.F.R. 1201.137(b). The Board has delegated authority to issue initial decisions in ALJ-removal proceedings to its own ALJs, see 5 C.F.R. 1201.140(a), or to an ALJ detailed to the Board from another agency, see 5 U.S.C. 3344; 5 C.F.R. 930.208. On exercise of such authority, the Board's ALJ conducts a hearing on the record to determine whether the agency has shown good cause for the penalty selected. Upon

finding by a preponderance of the evidence that the employing agency has shown good cause for removal, the Board's ALJ will issue an initial decision authorizing the employing agency to remove the ALJ. See 5 C.F.R. 1201.140(b) (describing procedure for good cause determination); 5 C.F.R. 1201.56(b)(1)(i) (identifying burden and degree of proof). That initial decision is subject, upon a petition for review, to plenary review by the Board. See 5 C.F.R. 1201.140(a)(2).

Issuance of the Board's final decision, if adverse to the ALJ, marks the effective date of the ALJ's removal (or other disciplinary action). Final decisions of the Board are subject to judicial review in the Federal Circuit at the behest of an aggrieved ALJ. See 5 U.S.C. 7703; 5 C.F.R. 1201.141. The employing agency has no appeal as of right from an adverse Board decision. But the Director of the Office of Personnel Management may petition for review in the Federal Circuit. 5 U.S.C. 7703(d)(1). Whether to accept such a petition from the Director "shall be at the discretion of the Court of Appeals." *Ibid.*

3. Petitioners were registered investment advisers who marketed a wealth-management strategy that they called "Buckets of Money," under which retirement savings were divided among assets of different risk levels (*e.g.*, bonds, fixed annuities, and stocks) and periodically reallocated as those assets changed in value. Pet. App. 38a, 41a, 127a. The Commission instituted administrative proceedings against petitioners based on allegations that petitioners had used misleading slideshow presentations to deceive prospective clients. *Id.* at 41a-51a. The Commission charged petitioners with violating the Securities Exchange Act, the Investment Advisers Act, and the Investment Company Act. *Id.* at 238a.

a. The Commission assigned the initial stages of the proceeding to an ALJ, who conducted a hearing that lasted nine days. Pet. App. 116a. The ALJ presided over witness testimony and cross-examinations, admitted documentary evidence, and ruled on objections. Pet. 5. In so doing, the ALJ established "the official record" of the administrative proceeding. Pet. App. 117a n.2.

After the hearing, the ALJ issued an initial decision finding that petitioners had made fraudulent misrepresentations related to one of their investment strategies; the ALJ did not, however, make factual findings regarding the remaining claims. Pet. App. 117a. The Commission then remanded to the ALJ for fact-finding on the three remaining claims, noting the "vital role that initial decisions play in the Commission's decisional process." *Id.* at 241a. The Commission explained that a determination by the ALJ as to the remaining claims would be of "considerable importance" because the Commission itself had not "observed the parties and witnesses." *Ibid.*

On remand, the ALJ issued a revised initial decision finding that petitioners had willfully and materially misled investors, in violation of the Investment Advisers Act. Pet. App. 195a-225a. The decision ordered a variety of sanctions to be imposed on petitioners, including revocation of their registrations as investment advisers; a permanent bar on associating with investment advisers, brokers, or dealers; a cease-and-desist injunction against future violations; and a total of $300,000 in civil monetary penalties. *Id.* at 235a; see *id.* at 225a-233a.

b. On appeal, the Commission conducted "an independent review of the record, except with respect to those findings not challenged on appeal." Pet. App. 40a.

The Commission determined that the ALJ had correctly found that petitioners, in marketing their Buckets of Money strategy, willfully made fraudulent statements and omissions in violation of the Investment Advisers Act. *Id.* at 66a-86a. The Commission also largely "affirm[ed]," with limited exceptions, "the sanctions imposed below" by the ALJ. *Id.* at 95a; see *id.* at 95a-107a. Commissioners Gallagher and Piwowar dissented with respect to one aspect of the Commission's liability determination. *Id.* at 110a-114a.

Petitioners argued before the Commission that the proceedings against them were unlawful because the ALJ who had conducted the hearing and issued the initial decision was an "Officer[] of the United States" within the meaning of the Appointments Clause, U.S. Const. Art. II, § 2, Cl. 2. See Pet. App. 86a. Petitioners noted that the ALJ had not been appointed, in accordance with that provision, "by the President, the head of a department, or a court of law." *Id.* at 87a. The Commission rejected petitioners' argument. In the Commission's view, its ALJs were mere employees rather than constitutional officers because they do not exercise "significant authority independent of the [Commission's] supervision." *Id.* at 88a; cf. *Buckley* v. *Valeo*, 424 U.S. 1, 126 n.162 (1976) (per curiam) (employees are "lesser functionaries subordinate to officers").

Among other things, the Commission explained, its ALJs "issue 'initial decisions' that are * * * not final," Pet. App. 88a-89a; a person aggrieved by an initial decision may seek review before the Commission, which "grant[s] virtually all petitions for review," *id.* at 89a (citation omitted); the Commission may review any ALJ decision *sua sponte*, *ibid.*; review of an ALJ's decision is *de novo*, *id.* at 90a-91a; and under the Commission's

rules, "no initial decision becomes final simply on the lapse of time by operation of law," but instead becomes final only upon "the Commission's issuance of a finality order," *id.* at 90a (citation and internal quotation marks omitted). The Commission also distinguished this Court's decision in *Freytag* v. *Commissioner*, 501 U.S. 868 (1991), in which special trial judges of the Tax Court were determined to be inferior officers under the Appointments Clause. Pet. App. 92a-93a.

4. On appeal of the Commission's order, a panel of the court of appeals denied the petition for review. Pet. App. 3a-36a. The court first rejected petitioners' Appointments Clause challenge, holding that the Commission's ALJs are mere employees rather than officers under the Clause because they do not exercise "significant authority pursuant to the laws of the United States." *Id.* at 11a (quoting *Buckley*, 424 U.S. at 126). For that conclusion, the court rested on its previous decision in *Landry* v. *FDIC*, 204 F.3d 1125, 1133-1134 (D.C. Cir.), cert. denied, 531 U.S. 924 (2000), which held that ALJs of the Federal Deposit Insurance Corporation did not exercise significant authority because they could not issue final decisions on behalf of the agency. See Pet. App. 12a. The court deemed it similarly dispositive here, in determining the constitutional status of the Commission's ALJs, that their initial decisions are non-final. *Id.* at 13a-19a.

The court of appeals further rejected petitioners' attempt to equate the Commission's ALJs with the special trial judges of the Tax Court who were held to be officers in *Freytag*. The special trial judges were distinguishable in the court of appeals' view because, as "members of an Article I court," they "could exercise the judicial power of the United States" and could "issue

final decisions in at least some cases." Pet. App. 11a-12a. The court of appeals also found special trial judges to be different than the Commission's ALJs because "the Tax Court in *Freytag* was required to defer to the special trial judge's factual and credibility findings unless they were clearly erroneous." *Id.* at 19a (citation and internal quotation marks omitted). The Commission, by contrast, "is not required to adopt the credibility determinations of an ALJ." *Ibid.*

On the merits, the court of appeals determined that substantial evidence supported the Commission's liability findings, Pet. App. 21a-32a, and that the Commission had not abused its discretion in ordering sanctions against petitioners, *id.* at 33a-36a.

5. Petitioners sought rehearing en banc, which the court of appeals granted on February 16, 2017. Pet. App. 244a-246a. On June 26, 2017, the en banc court issued a per curiam judgment denying the petition for review "by an equally divided court." *Id.* at 1a-2a.

SUMMARY OF ARGUMENT

Under Article II, only a properly appointed officer, whose exercise of executive power is subject to appropriate presidential supervision, may exercise significant governmental authority of the type entrusted by law to the ALJ in this case.

I. The Appointments Clause provides the exclusive method for appointment of "Officers of the United States," a term that includes public officials who "exercis[e] significant authority pursuant to the laws of the United States." *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam). The Commission's ALJs perform important functions in service of the execution of the Nation's securities laws: They preside over hearings, rule on motions, and create the administrative record. At

the conclusion of those hearings, ALJs issue initial decisions that interpret and apply the law; if not further reviewed, their decisions are "deemed the action of the Commission." 15 U.S.C. 78d-1(c). They accordingly exercise significant governmental authority, of a type substantially similar to the authority exercised by the special trial judges of the Tax Court found to be inferior officers in *Freytag* v. *Commissioner*, 501 U.S. 868 (1991). The Commission's ALJs are thus "inferior Officers" within the meaning of the Clause.

The nature of the authority exercised by the Commission's ALJs confirms that they are constitutional officers, rather than mere employees. Congress, in enacting the Administrative Procedure Act, deliberately chose to model the relationship between an agency and its "hearing examiners" (precursors to modern ALJs) on the relationship between appellate and trial courts. This Court's cases have similarly recognized the close parallel, in terms of functions and powers, between ALJs who preside over adversarial hearings and district judges. The Commission's ALJs also administer securities laws that permit the imposition of civil monetary penalties on registered or unregistered persons, powers that traditionally have been available only in district-court proceedings.

The panel below based its contrary conclusion almost entirely on the inability of ALJs to render final decisions. Giving that factor dispositive weight, however, is inconsistent with this Court's decision in *Freytag*, where the special trial judges were found to be inferior officers even though many of their decisions were subject to further review. The panel's single-minded focus on finality is also inconsistent with *Edmond* v. *United States*, 520 U.S. 651 (1997), which treated final decision-

making authority as a factor bearing on the dividing line between principal and inferior officers, not the line between inferior officers and employees. Finally, the Commission routinely affords substantial deference to ALJ credibility determinations, further confirming the significance of the role ALJs perform.

As inferior officers, the Commission's ALJs should have been appointed, in conformance with the Appointments Clause, by the Commission (as the Head of Department). But the ALJ who presided over petitioners' case was selected by the Commission's Chief ALJ, not the Commission itself, and his appointment was therefore invalid.

II. Because the Commission's ALJs possess significant authority, of the type that can only be exercised by a constitutional officer, a question arises regarding the statutory constraints that exist on removing them from office. The Court should address the removal issue now, to prevent a prolonged period of uncertainty regarding the authority of ALJs—whether or not properly appointed—to continue serving in agencies throughout the government.

This Court has permitted some tenure protections for inferior officers. But it has invalidated, as inconsistent with the President's responsibility to faithfully execute the laws, statutory restrictions that prevent adequate supervision of those who wield significant authority within the Executive Branch.

Under 5 U.S.C. 7521(a), an ALJ may be removed by an agency head "only for good cause established and determined by the Merit Systems Protection Board on the record after opportunity for hearing before the Board." Under the constitutional avoidance canon, this Court should construe Section 7521 to permit agency heads to

remove ALJs in a manner that ensures a constitutionally adequate level of Executive Branch supervision. In particular, the "good cause" for removing an ALJ is properly read to include an ALJ's misconduct or failure to follow lawful directives or to perform adequately. That interpretation would not permit removal of an ALJ for a legally prohibited reason, or to direct the result in a particular case. But it would ensure that ALJs could be held sufficiently accountable, even in independent agencies, for failure to execute the laws properly. For similar reasons, the Court should hold that cause "established and determined by the Merit Systems Protection Board" means that, rather than substitute its own judgment for that of the agency, the MSPB should confine its role to determining whether evidence exists to support the agency's view that "good cause" as defined above exists.

Thus interpreted, Section 7521 would leave the President with constitutionally adequate authority to ensure that ALJs are faithfully executing the law. If the Court determines that this interpretation cannot be reconciled with the statute, however, it should invalidate and sever the portion that cannot be interpreted to avoid unconstitutional interference with the President's supervision of the Executive Branch. Any further constitutional concerns, regarding Section 7521's requirement that removal may occur only "after opportunity for hearing before the Board," can be addressed in appropriate cases between employing agencies and their ALJs, because the timing of removal rather than suspension with pay does not affect the rights of private parties appearing before ALJs.

ARGUMENT

The Appointments Clause safeguards the President's ability to faithfully execute the laws by making governmental officials who wield significant executive authority accountable to the President. The Commission's ALJs, who preside over complex adversarial disputes and issue initial decisions that often become the final decisions of the agency, wield significant authority on behalf of the United States. They are thus "inferior Officers" who must be appointed in conformance with the Appointments Clause. Statutory restrictions on removing the Commission's ALJs likewise must be construed, under separation-of-powers principles, to afford appropriate presidential supervision.

The government took the position before the court of appeals that the Commission's ALJs are mere employees, rather than constitutional officers. Upon further consideration, and in light of the implications for the exercise of executive power under Article II, the government is now of the view that such ALJs are officers because they exercise "significant authority pursuant to the laws of the United States." *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam). The government has reassessed the importance of the functions that ALJs perform, as well as the proper interpretation of this Court's decision in *Freytag* v. *Commissioner*, 501 U.S. 868 (1991), which held that adjudicative officials exercising similar functions were inferior officers for purposes of the Appointments Clause.

I. THE COMMISSION'S ALJs ARE CONSTITUTIONAL OFFICERS SUBJECT TO THE APPOINTMENTS CLAUSE

The Constitution vests "[t]he executive Power" of the United States in the President, U.S. Const. Art. II, § 1, Cl. 1, who is charged with responsibility to "take

Care that the Laws be faithfully executed," *id.* § 3. The Framers, however, recognized that, "in a republican government," the President would need to rely on the assistance of subordinate officials "to give dignity, strength, purity, and energy to the administration of the laws." 3 Joseph Story, *Commentaries on the Constitution of the United States* § 1524, at 376 (1833). To govern effectively, the President must be able to depend upon others to carry out his responsibility for faithful execution of the laws and thus to exercise a portion of the sovereign authority of the United States, including the power to "bind third parties, or the government itself, for the public benefit." *Officers of the United States Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73, 87 (2007) (2007 OLC Mem.). The Constitution accordingly provides for the creation of public offices "established by Law" and for the appointment of "Officers of the United States." U.S. Const. Art. II, § 2, Cl. 2.

A. The Appointments Clause Prescribes The Manner For Selecting Officials Who Exercise "Significant Authority Pursuant To The Laws Of The United States"

1. "The 'manipulation of official appointments' had long been one of the American revolutionary generation's greatest grievances against executive power." *Freytag*, 501 U.S. at 883 (quoting Gordon S. Wood, *The Creation of the American Republic 1776-1787*, at 79 (1969)). The Framers therefore chose to "limit[] the appointment power," so as to "ensure that those who wielded it were accountable to political force and the will of the people." *Id.* at 884. Far from being a mere matter of "etiquette or protocol," *Buckley*, 424 U.S. at 125, limitations on the method of appointing public officials are "among the significant structural safeguards

of the constitutional scheme." *Edmond* v. *United States*, 520 U.S. 651, 659 (1997); see *Free Enter. Fund* v. *Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 498 (2010) ("Without a clear and effective chain of command, the public cannot determine on whom the blame or the punishment of a pernicious measure, or series of pernicious measures ought really to fall.") (citation and internal quotation marks omitted).

The Appointments Clause, U.S. Const. Art. II, § 2, Cl. 2, provides the only method by which "Officers of the United States" may be appointed. For "principal Officer[s]," they must be appointed by the President, by and with the advice and consent of the Senate. *Id.* Cls. 1, 2. The same manner of appointment applies to "inferior Officers"—*i.e.*, those "whose work is directed and supervised at some level by others who were appointed by Presidential nomination with the advice and consent of the Senate," *Edmond*, 520 U.S. at 663—except where their appointments have instead been vested by law "in the President alone, in the Courts of Law, or in the Heads of Departments." U.S. Const. Art. II, § 2, Cl. 2. These appointment methods, for principal and inferior officers, are exhaustive: "[A]ll persons who can be said to hold an office under the government * * * were intended to be included within one or the other of these modes of appointment." *United States* v. *Germaine*, 99 U.S. 508, 510 (1879).

The constraints of the Appointments Clause, however, do not apply to the entire federal workforce. One may be "an agent or employé working for the government and paid by it * * * without thereby becoming its officer[ ]." *Germaine*, 99 U.S. at 509. Much of the work of the Executive Branch is performed by non-officer "employees"—that is, by "lesser functionaries" whose

work is overseen by officers and who need not themselves be appointed pursuant to the Appointments Clause. *Buckley*, 424 U.S. at 126 n.162. This Court recently estimated that the percentage of federal employees and agents who are *not* officers "dramatically" exceeds 90%. *Free Enter. Fund*, 561 U.S. at 506 n.9; see *Germaine*, 99 U.S. at 509 ("nine-tenths of the persons rendering service to the government undoubtedly are" not officers).

2. Although distinguishing between constitutional officers and mere employees is not always straightforward, this Court has provided guidance. In *Buckley*, the Court explained that "any appointee exercising significant authority pursuant to the laws of the United States is an 'Officer of the United States,' and must, therefore, be appointed in the manner prescribed by" the Appointments Clause. 424 U.S. at 126 (citation omitted). That description—and its focus on "significant" governmental authority—reflects the common understanding at the time of the Founding that "[a] public office is the right, authority and duty, created and conferred by law, by which for a given period * * * an individual is invested with some portion of the sovereign functions of government, to be exercised by him for the benefit of the public." Floyd R. Mechem, *A Treatise on the Law of Public Offices and Officers* § 1, at 1-2 (1890) (summarizing English and early American sources); see 2007 OLC Mem. 84-87.[3]

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[3] Not all officials who wield significant authority require appointment in conformity with the Appointments Clause. To qualify as a constitutional officer, one also must occupy a continuing office established by law. See 2007 OLC Mem. 100; see also *Freytag*,

The nature of significant authority was addressed in *Freytag*. There, the Court considered whether special trial judges of the Tax Court were inferior officers rather than employees. The special trial judges were appointed by the Chief Judge and were authorized to hear certain proceedings specified by law, see 26 U.S.C. 7443A(b) (1988), as well as other proceedings designated by the Chief Judge. See 501 U.S. at 870-871. In the specified proceedings, the special trial judges were authorized to issue final decisions. 26 U.S.C. 7443A(c) (1988). But in other designated proceedings, they could only "prepare proposed findings and an opinion" for a Tax Court judge, who would render the "actual decision." 501 U.S. at 873.

The petitioners in *Freytag* were taxpayers who had objected to tax deficiencies assessed against them and sought review in the Tax Court. 501 U.S. at 870-871. The Chief Judge designated the case to be heard by a special trial judge, who was assigned to "preside over the trial as evidentiary referee" and "for preparation of written findings and an opinion." *Id.* at 871. Ultimate "disposition" of the case, however, was reserved for the Chief Judge, who "had the duty to review the work of the Special Trial Judge." *Id.* at 872 n.2. Following an adverse decision by the special trial judge and an unsuccessful appeal to the Chief Judge, the petitioners "contended that the assignment of cases as complex as

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501 U.S. at 881 (Appointments Clause does not apply to special masters hired on a "temporary, episodic" basis); *Germaine*, 99 U.S. at 511-512 (noting relevance of office's "tenure" and "duration," including whether official's duties are "continuing and permanent, not occasional or temporary"). There is no dispute in this case that the Commission's ALJs occupy continuing positions established by law. See pp. 3-6, *supra*.

theirs to a special trial judge" in the first instance "violated the Appointments Clause of the Constitution." *Id.* at 872.

In addressing that claim, this Court rejected the government's argument that "special trial judges may be deemed employees," rather than constitutional officers, "because they lack authority to enter a final decision." *Freytag*, 501 U.S. at 881. That argument, the Court explained, "ignores the significance of the duties and discretion that special trial judges possess." *Ibid.* Unlike special masters, who are hired "on a temporary, episodic basis" to perform ad hoc tasks, the Court reasoned, special trial judges occupy an office "'established by Law,'" and the "duties, salary, and means of appointment for that office are specified by statute." *Ibid.* (quoting U.S. Const. Art. II, § 2, Cl. 2). Moreover, the Court emphasized, special trial judges, in presiding over preliminary proceedings, "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders." *Id.* at 881-882. "In the course of carrying out these important functions," the Court concluded, "special trial judges exercise significant discretion." *Id.* at 882.

The Court went on to hold in the alternative that special trial judges would qualify as constitutional officers "[e]ven if" their ability to issue initial decisions in cases like the petitioners' were not so "significant." *Freytag*, 501 U.S. at 882; see *ibid.* ("[O]ur conclusion would be unchanged."). That is because, the Court explained, special trial judges were also authorized by law to "render the decisions of the Tax Court [*i.e.*, final decisions] in declaratory judgment proceedings and limited-amount tax cases." *Ibid.* Since it was not disputed that "a special trial judge is an inferior officer for purposes

of" those proceedings, the Court concluded that their appointments must comply with the Appointments Clause for all purposes. *Ibid.* ("Special trial judges are not inferior officers for purposes of some of their duties * * * but mere employees with respect to other responsibilities.").

B. The Commission's ALJs Exercise "Significant Authority"

The Commission's ALJs "closely resemble" the special trial judges at issue in *Freytag*. *Bandimere* v. *SEC*, 844 F.3d 1168, 1181 (10th Cir. 2016), petition for cert. pending, No. 17-475 (filed Sept. 29, 2017). Like the special trial judges, ALJs occupy a position fixed by law. See 5 U.S.C. 3105 (appointment authority), 5372(b) (compensation). They preside over trial-like hearings in which they control the conduct of the parties for the adjudication of charges seeking sanctions for violations of provisions regulating their primary conduct. They rule on motions and shape the record; and at the hearings' conclusion, ALJs issue rulings that interpret and apply the law to the facts as found, often rendering decisions that are deemed to be on behalf of the Commission itself. These ALJs accordingly "exercis[e] significant authority pursuant to the laws of the United States," *Buckley*, 424 U.S. at 126, as several Members of the Court previously have recognized. See *Free Enter. Fund*, 561 U.S. at 542 (Breyer, J., dissenting, joined by Stevens, Ginsburg, and Sotomayor, J.J.); *Freytag*, 501 U.S. at 910 (Scalia, J., concurring in part and concurring in the judgment, joined by O'Connor, Kennedy, and Souter, J.J.).

1. An ALJ who adjudicates a dispute on behalf of the Commission performs important executive functions

The Commission's ALJs preside over adversarial proceedings through a grant of significant authority "delegate[d]" from the Commission. 15 U.S.C. 78d-1(a). The Commission's ALJs are authorized, among other things, to administer oaths, hold hearings, take testimony and admit evidence, issue or quash subpoenas, rule on motions, impose sanctions on contemptuous hearing participants, reject deficient filings, and enter default judgments. See 17 C.F.R. 201.111(a), (b), (c), and (h), 201.180(a)-(c). Thus, like the special trial judges in *Freytag*, the Commission's ALJs "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders. In the course of carrying out these important functions, [they] exercise significant discretion." 501 U.S. at 881-882.[4] At the conclusion of a hearing, the ALJ issues an "initial decision" that "include[s] findings and conclusions * * * as to all the material issues of fact, law or discretion presented on the record

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[4] Although the Tax Court in *Freytag* was authorized to "punish contempts by fine or imprisonment," 501 U.S. at 891 (citing 26 U.S.C. 7456(c)), the Commission and its ALJs have the authority to punish "[c]ontemptuous conduct" only by "[e]xclud[ing]" the contemnor from the deposition or hearing or by "[s]ummarily suspend[ing] that person from representing others in the proceeding." 17 C.F.R. 201.180(a)(1). This Court's "officer" holding in *Freytag*, however, relied on the special trial judges' "power to enforce compliance with discovery orders," not on the particular type of contempt sanction available. 501 U.S. at 882. This Court invoked the specific power to fine or imprison only in support of its subsequent holding that the Tax Court was a "'Court of Law' within the meaning of the Appointments Clause." *Id.* at 890 (brackets omitted); see *id.* at 890-891.

and the appropriate order, sanction, relief, or denial thereof." 17 C.F.R. 201.360(b).

In some instances, moreover, an initial ALJ decision becomes the final decision for the Commission itself. Under the Commission's organic statute, if further review of the ALJ's decision is not sought, or if a request for such review is denied by the Commission, the ALJ's initial decision "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. 78d-1(c). To be sure, the Commission has, by regulation, adopted a policy that in cases in which plenary review by the Commission does not occur, the Commission "will issue an order" of its own confirming that the ALJ's decision has become final. 17 C.F.R. 201.360(d)(2). But the ALJ's initial decision is still "deemed" by statute to be "the action of the Commission"; the finality order, by definition, issues only when the Commission has *not* engaged in plenary review of the ALJ's decision. The vast majority of ALJ decisions (approximately 90%), which often involve default findings or other uncontested decisions, are not reviewed on the merits by the Commission, and thus the initial decision authored by the ALJ functions as the final decision of the Commission. See *Bandimere*, 844 F.3d at 1184 n.36, 1187 n.41.[5]

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[5] Notwithstanding the Commission's finality-order regulation, for many years its ALJs issued self-executing default orders in cases in which the respondent failed to appear. See *In re Alchemy Ventures, Inc.*, Exchange Act Release No. 70,708, 2013 WL 6173809 (Oct. 17, 2013) (describing and disapproving of this practice). In those cases, the ALJ's default order became the final and enforceable decision of the agency without *any* additional action by the Commission, a practice that the Commission has disavowed.

The significance of the ALJs' decision-making authority is further underscored by the fact that, in most cases, adversely affected parties do not have any statutory or regulatory entitlement to review by the Commission. Agency regulations make Commission review mandatory when sought in a few specified types of cases, 17 C.F.R. 201.411(b)(1), but in most instances, Commission review is "[d]iscretionary" and the "Commission may decline to [grant] review," 17 C.F.R. 201.411(b)(2) (emphasis omitted). Earlier in this litigation, the government emphasized that the Commission has voluntarily assumed the practice of granting merits review in all cases where it is timely sought. See Pet. App. 89a. But the Commission's practice—which is not mandated by any statute or regulation—does not alter the fact that the Commission's ALJs are authorized to issue decisions that can become final decisions of the agency even where a sanctioned party wishes to challenge the ALJ's determination on the merits before the Commission.

The fact that the Commission may choose to grant plenary review of the ALJ's initial decision, as it did in this case, does not undermine the conclusion that the Commission's ALJs possess significant authority of the type required to be exercised by a constitutional officer. *Freytag* recognized that it is not possible for public officials to be "inferior officers for purposes of some of their duties * * * but mere employees with respect to other responsibilities." 501 U.S. at 882. The "significant" authority exercised by the Commission's ALJs in cases where their decisions are not further reviewed makes them constitutional officers even if, in other cases, they wield a lesser form of authority. *Ibid.*

In any event, ALJs exercise significant authority even when the Commission grants plenary review of their initial decisions. As explained above, rather than acting as mere "aid[es]" to the ultimate decision-maker, the Commission's ALJs "exercise significant discretion" in the course of carrying out "important functions" that closely resemble those performed by the special trial judges in *Freytag*. 501 U.S. at 880, 882; see *id.* at 881-882. Indeed, the Commission in this case recognized the "vital role that initial decisions play in the Commission's decisional process." Pet. App. 241a. It explained that the Commission affords an ALJ's determination "considerable importance," because the Commission itself has not "observed the parties and witnesses" and the ALJ "is in the best position to make findings of fact, including credibility determinations, and resolve any conflicts in the evidence." *Ibid.*; see *Universal Camera Corp.* v. *NLRB*, 340 U.S. 474, 496 (1951) (recognizing that ALJ "decisions [are] of consequence, for example, to the extent that material facts in any case depend on the determination of credibility of witnesses as shown by their demeanor or conduct at the hearing") (citation and internal quotation marks omitted).

Finally, the government notes that it does not rely, as petitioners have, on nineteenth-century decisions of this Court concluding that an array of comparatively unimportant positions are "offices." See, *e.g.*, Pet. 11-12. These early decisions were primarily concerned with the question whether Congress *intended* to treat a position it had created by statute as an "office," not whether the functions of the position were so significant that the Constitution *required* that the position be held by an officer appointed pursuant to the Appointments

Clause.[6] The Court therefore looked at whether the appointment had occurred in the manner contemplated by the Clause as evidence of whether Congress intended to treat the appointee as an officer. These decisions, however, do not themselves speak to whether the Commission's ALJs exercise significant authority of the type that can only be possessed by a properly appointed constitutional officer. Instead, that inquiry turns on whether ALJs exercise significant governmental authority, which they do for the reasons stated above.

2. In presiding over proceedings of the Commission, an ALJ serves a role comparable to that of a trial judge

When Congress in 1946 enacted the Administrative Procedure Act (APA), ch. 324, 60 Stat. 237 (5 U.S.C. 551 *et seq.*), it used trial courts as a model for the position that became the modern ALJ—a parallel that has only strengthened over time, as ALJs have been given powers that previously could only have been exercised by district courts. Those similarities further confirm that the Commission's ALJs exercise significant authority for purposes of the Appointments Clause.

a. The strong parallel between ALJs and Article III judges exists by congressional design. Prior to the APA, administrative agencies relied on hearing "examiners" who, along with other employees, performed various tasks to assist in assembling the administrative record. See Act of June 29, 1906, ch. 3591, 34 Stat. 595

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[6] See, *e.g.*, *Germaine*, 99 U.S. at 509 (civil surgeon could not be prosecuted under criminal statute applicable only to an "officer of the United States who is guilty of extortion") (citation omitted); *United States* v. *Hartwell*, 73 U.S. (6 Wall.) 385, 391-392 (1868) (statute forbidding embezzlement by "officers" applied to clerk appointed by the assistant treasurer in Boston with the approbation of the Acting Secretary of the Treasury).

(authorizing the Interstate Commerce Commission "to employ special agents or examiners who shall have power to administer oaths, examine witnesses, and receive evidence"); see also, *e.g.*, Act of Sept. 26, 1914, ch. 311, 38 Stat. 718 (Federal Trade Commission); Act of Sept. 7, 1916, ch. 451, 39 Stat. 729 (United States Shipping Board). Their powers were limited. For example, the Commission's hearing examiners were permitted to "rule on contested motions for postponement, continuance and the time and place of hearings," but "[a]ll other motions [could] be ruled on only by the Commission." S. Doc. No. 8, 77th Cong., 1st Sess. 395-396 (1941) (*Attorney General's Report*). Although the Commission's rules of practice authorized hearing examiners to file reports containing findings of fact, they generally did "not permit inclusion of conclusions of law or recommendations in the report," though this restriction was not followed in all cases. *Id.* at 396. The Commission itself reexamined all hearing-examiner reports *de novo*, regardless whether exceptions had been filed, and the Commission "regard[ed] the report as advisory only" and entitled to "little weight." *Ibid.*

Over time, however, as administrative proceedings proliferated, agencies came increasingly to rely on their hearing examiners to engage in more substantive work. As a task force created by the Attorney General explained, in such a role the hearing examiner was "in a very real sense acting for the head of the agency. He is hearing cases because the heads cannot as a practical matter themselves sit. He plays an essential part in the process of hearing and deciding." *Attorney General's Report* 47. Congress thus recognized the need for a for-

malized legal framework to "increase the power and status of hearing officers." 2 Kenneth Culp Davis, *Administrative Law Treatise* § 10.01 (1958).

The APA codified the office and functions of the administrative hearing examiner—the position now called ALJ. Consistent with Congress's understanding that hearing officers would perform a critical role in formal agency adjudications, Section 7 of the APA required that certain administrative hearings be presided over only by "(1) the agency, (2) one or more members of the body which comprises the agency, or (3) one or more examiners appointed as provided in this Act." 60 Stat. 241 (codified as amended at 5 U.S.C. 556(b)). Congress thus made clear the importance of hearing examiners by classifying them, along with the agency heads themselves, as the only individuals authorized to hold such hearings under the APA.

Congress also took steps to preserve the independence of the new hearing examiners, in response to the criticism that hearing examiners had previously been "mere tools of the agency concerned and subservient to the agency heads in making their proposed findings of fact and recommendations." *Ramspeck* v. *Federal Trial Exam'rs Conference*, 345 U.S. 128, 131 (1953). In Section 7(b) of the APA, Congress adopted the recommendation of the Attorney General's task force, which had advocated "fully empower[ing]" hearing examiners "by statute to preside at hearings, issue subpoenas, administer oaths, rule upon motions, carry out other duties incident to the proper conduct of hearings, and make findings of fact, conclusions of law, and orders for the disposition of matters coming before them." *Attorney General's Report* 50; see APA § 7, 60 Stat. 241 (enumer-

ating presiding officer's "hearing powers") (capitalization altered). As the House Committee explained, Section 7(b) "assures that the presiding officer or officers will perform a real function rather than serve merely as notaries or policemen." S. Doc. No. 248, 79th Cong., 2d Sess. 269 (1946); see *ibid.* ("They would have and independently exercise all the powers listed in the section."); see also *Universal Camera Corp.*, 340 U.S. at 496 (Congress intended to "g[i]ve significance to the findings of examiners"). The provision was intended to ensure that the agency itself did not "in effect conduct hearings from behind the scenes where it cannot know the detailed happenings in the hearing room and does not hear or see the witnesses or private parties." S. Doc. No. 248, at 269; see *id.* at 207.

Section 8 provided, in turn, that when the agency itself has not presided over the hearing, the hearing examiner's initial decision, "in the absence of either an appeal to the agency or review upon motion of the agency within time provided by rule, * * * shall without further proceedings then become the decision of the agency." APA § 8, 60 Stat. 242 (codified as amended at 5 U.S.C. 557(b)). This provision appears to reflect a recommendation by the Attorney General's task force that the relationship between a hearing examiner and the agency should be similar in many respects to "that of trial court to appellate court." *Attorney General's Report* 51; see S. Doc. No. 248, at 272 ("In a broad sense the agencies' reviewing powers are to be compared with that of courts."); see also *Universal Camera*, 340 U.S. at 495 (describing recommendation's influence on Congress). The hearing examiner's decision serves "as the initial adjudication of most cases, and the final adjudication in many, just as does the decision of a trial court."

Attorney General's Report 51. Congress also recognized that a hearing examiner's initial or recommended decision would have special importance where credibility was at issue. Congress contemplated "that agencies will attach considerable weight to the findings of the examiner who saw and heard the witnesses." *Attorney General's Manual on the Administrative Procedure Act* 84 (1947); see S. Doc. No. 248, at 272 (initial and recommended decisions "become a part of the record and are of consequence, for example, to the extent that material facts in any case depend on the determination of credibility of witnesses as shown by their demeanor or conduct at the hearing").

The history of the APA thus makes clear that Congress intended for hearing examiners, the precursors to ALJs, to perform a significant and independent role in the adjudicative process, notwithstanding the fact that their decisions typically would be subject to further agency review. Although congressional intent is not dispositive of the constitutional question here, it reinforces the conclusion that the authority exercised by ALJs is—and was intended to be—significant.

b. This Court has recognized, in two related contexts, the similarity of the role played by ALJs in presiding over administrative hearings to the role performed by district judges in judicial proceedings. In *Butz* v. *Economou*, 438 U.S. 478 (1978), the Court held that ALJs are entitled to absolute immunity from damages actions, rather than the qualified immunity normally available to Executive Branch officials. The Court reached that conclusion based on its view "that adjudication within a federal administrative agency shares * * * characteristics of the judicial process." *Id.*

at 512-513. "There can be little doubt," the Court explained, "that the role of the modern federal hearing examiner or administrative law judge within this framework is functionally comparable to that of a judge." *Id.* at 513 (internal quotation marks omitted). In presiding over proceedings that are "adversary in nature," an ALJ enjoys "powers [that] are often, if not generally, comparable to those of a trial judge: He may issue subpoenas, rule on proffers of evidence, regulate the course of the hearing, and make or recommend decisions." *Ibid.* And, "importantly, the process of agency adjudication is currently structured so as to assure that the hearing examiner exercises his independent judgment on the evidence before him, free from pressures by the parties or other officials within the agency." *Ibid.*; see *id.* at 514 ("When conducting a hearing * * * a hearing examiner is not responsible to, or subject to the supervision or direction of, employees or agents engaged in the performance of investigative or prosecution functions for the agency.").

This Court also relied upon the parallel between agency adjudications and court proceedings in *Federal Maritime Commission* v. *South Carolina State Ports Authority*, 535 U.S. 743 (2002), in holding that a State could assert sovereign immunity in a proceeding of the Federal Maritime Commission (FMC), just as it could in a judicial proceeding. In so ruling, the Court found "the similarities between FMC proceedings and civil litigation [to be] overwhelming," explaining that "the role of the ALJ, the impartial officer designated to hear a case, is similar to that of an Article III judge." *Id.* at 758-579 (citation and footnote omitted). Among other things, the Court noted that an FMC ALJ had authority to arrange for a hearing at which the ALJ determined

the presentation of evidence, disposed of procedural motions, heard and ruled on substantive motions, administered oaths, examined witnesses, and ruled on the admission of evidence. *Ibid.* Those, of course, are the same functions performed by the Commission's ALJs. See 17 C.F.R. 201.111.

c. The functions exercised by the Commission's ALJs also have grown over time to more closely resemble those of trial judges. Early in its history, the Commission's authority to bring an administrative proceeding or to issue sanctions was relatively limited. As initially created, the Commission could only obtain a "stop order" suspending a securities registration statement and thus halting a public securities offering under Section 8 of the Securities Act of 1933. 48 Stat. 79-80 (codified as amended at 15 U.S.C. 77h). Congress later authorized the Commission to deny or revoke the registration of a broker-dealer under the Securities Exchange Act of 1934, §§ 14-18, 48 Stat. 895-898 (codified as amended at 15 U.S.C. 78*o*), or of an investment adviser under the Investment Advisers Act of 1940, § 203, 54 Stat. 850 (codified as amended at 15 U.S.C. 80b-3). Congress then amended the Exchange Act to authorize the Commission to suspend or bar persons "associated with" broker-dealers, and it expanded the grounds for denying or revoking broker-dealer registrations. Securities Acts Amendments of 1964, Pub. L. No. 88-467, 78 Stat. 570-574; see Investment Company Amendments Act of 1970, Pub. L. No. 91-547, 84 Stat. 1431 (codified as amended at 15 U.S.C. 80b-3(f)) (adding similar authority to the Investment Advisers Act).

In 1990, Congress authorized the Commission—for the first time—to seek civil monetary penalties in enforcement proceedings against registered entities and

associated persons, Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, 104 Stat. 932 (codified at 15 U.S.C. 77t(d)), as well as to enter cease-and-desist orders against unregistered entities and persons, *id.* § 102, 104 Stat. 933-934. And in 2010, Congress further expanded the Commission's administrative enforcement authority, empowering the Commission to impose civil monetary penalties against unregistered entities. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 929P(a), 124 Stat. 1862. As the former Director of the Commission's Division of Enforcement explained, prior to Dodd-Frank, "penalties against unregulated entities or individuals were only available in district court. That legislative change allows us to obtain many —though not all—of the same remedies in administrative proceedings as we could get in district court." Andrew Ceresney, Director, SEC Division of Enforcement, U.S. SEC, *Remarks to the American Bar Association's Business Law Section Fall Meeting* (Nov. 21, 2014), https://www.sec.gov/news/speech/2014-spch112114ac.

Thus, the breadth and complexity of the proceedings that Congress has entrusted to the Commission have increased markedly since the Commission's inception. And as Congress has steadily increased the Commission's authority to proceed administratively against a wider array of individuals and businesses, and to impose more severe sanctions, the Commission has continued to rely on its ALJs to perform the bulk of the work associated with those proceedings, including compiling the record and issuing initial decisions regarding whether and what sanctions to impose. Today, the Commission's ALJs hear cases that a mere ten years ago could have appeared only in federal district courts.

C. The Reasons Given Below For Treating The Commission's ALJs As Employees Are Unpersuasive

A panel of the court of appeals nonetheless concluded that the Commission's ALJs are not constitutional officers. In so finding, the panel gave dispositive weight to its perception that those ALJs have no authority to issue final decisions that "bind third parties, or the government itself, for the public benefit." Pet. App. 12a-13a; see *id.* at 13a ("Our analysis begins, and ends, there."). The panel's conclusion is based on a misunderstanding about the function of the Commission's ALJs and is, in any event, legally erroneous.

1. The panel below relied on its prior decision in *Landry* v. *FDIC*, 204 F.3d 1125 (D.C. Cir.), cert. denied, 531 U.S. 924 (2000), which read *Freytag* as treating final decision-making authority as the key to officer status. Pet. App. 11a-13a. The Commission's ALJs, the panel asserted, cannot issue final decisions: An ALJ's initial decision "becomes final when, and only when, the Commission issues [a] finality order, and not before then." *Id.* at 15a.

In placing conclusive weight on the purported lack of final decision-making authority by the Commission's ALJs, the panel misread *Freytag*. The Court in *Freytag* principally held that special trial judges were properly considered officers because they carried out "important functions" and "exercise[d] significant discretion." 501 U.S. at 882; see *id.* at 881-882. The Court reached that conclusion *despite* an argument that the special trial judges "lack[ed] authority to enter a final decision" in the entire category of proceedings at issue there (those not statutorily specified). *Id.* at 881. Giving dispositive weight to the absence of final decision-making authority, the Court explained, would improperly "ignore[ ] the

significance of the duties and discretion that special trial judges possess." *Ibid.*

To be sure, the Court went on to say that special trial judges would be officers "[e]ven if" their authority over such cases were "not as significant as [the Court] * * * ha[d] found them to be," given their authority to render final decisions in other types of cases (the statutorily specified proceedings). *Freytag*, 501 U.S. at 882. But "the Court clearly designated [that statement] as an alternative holding." *Landry*, 204 F.3d at 1142 (Randolph, J., concurring in part and concurring in the judgment). The Court in *Freytag* thus indicated that final authority to make certain discretionary decisions may be sufficient, but is not necessary, to render an official an "Officer[ ] of the United States" within the meaning of the Appointments Clause. In light of the substantial authority wielded by the Commission's ALJs, see pp. 21-25, *supra*, they are constitutional officers even without regard to the authority to issue final decisions of the agency.

The panel's analysis is dubious on its own terms, moreover, because the Commission's ALJs *are* statutorily authorized to issue final decisions of the agency in many cases. Congress has provided that if review by the Commission is not sought or is denied, the ALJ's initial decision "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. 78d-1(c). An ALJ's initial decision thus serves by statute as the final—and only—agency decision in a significant percentage of cases. *Bandimere*, 844 F.3d at 1187 n.41. The panel rejected the relevance of that provision, noting that the Commission has adopted a regulation preventing the decisions of its

ALJs from taking effect until the Commission has issued a finality order of its own. See Pet. App. 14a-18a. But as noted above, the ALJ's decision is still the Commission's final decision by operation of statute, even if the ALJ's decision does not take effect until the Commission issues a finality order confirming the Commission's choice not to grant plenary review. See pp. 23-24, *supra*.

2. The panel's focus on finality as a means of distinguishing officers from mere employees also is at odds with this Court's decision in *Edmond*, which involved an Appointments Clause challenge to the judges on the Coast Guard Court of Criminal Appeals. The petitioners, whose convictions had been upheld by the Court of Criminal Appeals, argued that the court's decisions were invalid because its judges were principal officers who had not been appointed by the President with the advice and consent of the Senate. 520 U.S. at 655-656. This Court disagreed, concluding instead that the judges were inferior officers. *Id.* at 658-666. In reaching that conclusion, the Court noted that the judges had "no power to render a final decision on behalf of the United States unless permitted to do so by other Executive officers." *Id.* at 665. That fact was "significant," the Court explained, because it showed that the judges were supervised in the exercise of their authority by other Executive Branch officials, a clear sign that they were inferior, rather than principal, officers. *Ibid.*; see *id.* at 663. In *Edmond*, the Court thus held that the existence of final decision-making authority can be significant in drawing the dividing line between principal and inferior officers—not, as the panel below held, between constitutional officers and mere employees.

The panel below dismissed the relevance of *Edmond* on the ground that the government had conceded there that the judges were officers of some type, such that this Court "had no occasion to address the differences between employees and Officers." Pet. App. 13a. That reading of *Edmond* is unpersuasive. If the panel were correct that an official's lack of final decision-making authority automatically rendered that official an employee rather than an officer, the Appointments Clause challenge in *Edmond* would have been quite easy to resolve: Judges of the Court of Criminal Appeals did not have authority to render final decisions unless permitted to do so by other Executive Branch officers, and so (under the panel's reasoning) they could not be officers of any type, let alone principal officers. This Court nevertheless found them to be inferior officers only after considering a number of additional factors (tenure of office, jurisdiction, responsibilities, supervision by other officials, see 520 U.S. at 661-666), showing that the inability to render final decisions does not have the importance that the panel attributed to it.

3. In finding the Commission's ALJs to be mere employees, the panel below also mistakenly emphasized the relatively low level of deference afforded by the Commission to the decisions of its ALJs. The panel noted that the Commission "reviews an ALJ's decision *de novo* and 'may affirm, reverse, modify, or set aside' the initial decision, 'in whole or in part,' and it 'may make any findings or conclusions that in its judgment are proper and on the basis of the record.'" Pet. App. 18a-19a (quoting 17 C.F.R. 201.411(a)) (brackets omitted). The panel stressed that although the Commission has chosen to "defer to credibility determinations where the record provides no basis for disturbing the

finding," the Commission is "not required to adopt the credibility determinations of an ALJ." *Id.* at 19a. By contrast, the panel noted, "the Tax Court in *Freytag* was required to defer to the special trial judge's factual and credibility findings unless they were clearly erroneous." *Ibid.* (citation and internal quotation marks omitted).

The panel's proposed distinction of *Freytag* is unpersuasive. As the Commission noted in this very case, ALJ fact-finding usually will be given deference in practice because the ALJ "is in the best position to make findings of fact, including credibility determinations, and resolve any conflicts in the evidence." Pet. App. 241a. In any event, the level of deference afforded to the decisions of special trial judges in *Freytag* played no role in the Court's conclusion that they qualified as "Officers" within the meaning of the Appointments Clause. See 501 U.S. at 880-882. The Court mentioned deference in a different portion of its decision, addressing a distinct statutory-construction issue regarding the scope of the special trial judges' authority, and even there the Court stated that the "point [wa]s not relevant." *Id.* at 874 n.3.

There is similarly no merit to the panel's attempt to distinguish *Freytag* on the ground that the special trial judges at issue there were "members of an Article I court [who] could exercise the judicial power of the United States." Pet. App. 11a. *Freytag* did not mention the putative judicial status of special trial judges when considering whether they were officers. See 501 U.S. at 880-882. Only after the Court concluded that they were officers (in Part IV.B of its decision) did the Court go on to address whether the Tax Court was a "Court[] of law" within the meaning of the Appointments Clause (in

Part IV.C). See *id.* at 882 ("Having concluded that the special trial judges are 'inferior Officers,' we consider the substantive aspect of petitioners' Appointments Clause challenge."). Tellingly, although the Court was unanimous in holding that the special trial judges were constitutional officers, see *id.* at 901 (Scalia, J., concurring in part and concurring in the judgment) ("I agree with the Court that a special trial judge is an 'inferior Officer' within the meaning of this Clause.") (brackets omitted), the Court divided on the question whether special trial judges exercised judicial power, see *ibid.* ("I do not agree, however, with the Court's conclusion that the Tax Court is a 'Court of Law' within the meaning of this provision.") (brackets omitted). The former issue clearly did not turn on the latter.

D. The Appointment Of The ALJ In This Case Did Not Comply With The Appointments Clause

The ALJ who presided in petitioners' case was an inferior officer, but the method of his appointment did not conform to the Appointments Clause. That ALJ was selected by the Commission's Chief ALJ, subject to approval by the Commission's Office of Human Resources. See p. 3, *supra*. Neither the President nor the Commission itself, as the constitutional Head of Department, played any role in the selection or approval of the ALJ. See Pet. App. 295a-297a. Petitioners raised the Appointments Clause issue before the Commission and the court of appeals. The decision below affirming a ruling by the Commission that rejected the need for the Commission to appoint its ALJ should accordingly be reversed.

II. STATUTORY RESTRICTIONS ON REMOVAL OF THE COMMISSION'S ALJs MUST BE NARROWLY CONSTRUED IN LIGHT OF SERIOUS SEPARATION-OF-POWERS CONCERNS

The conclusion that the Commission's ALJs wield significant governmental authority, of the type that can only be exercised by constitutional officers, has implications for whether the statutory constraints on removing ALJs from office unconstitutionally impair the President's ability to faithfully execute the laws. See *Free Enter. Fund*, 561 U.S. at 504. Because the restraints on removing ALJs are statutory, a decision by this Court addressing only the requirements for appointing ALJs—but not the restrictions on removing them—would leave significant uncertainty surrounding the constitutionality of administrative proceedings conducted by the Commission and by other agencies throughout the government that use ALJs in adversarial proceedings. The public interest therefore strongly favors addressing the removal restraints in this case. To avoid serious constitutional concerns, the Court should construe the statutory provision that addresses tenure protections for ALJs, 5 U.S.C. 7521(a), to permit the removal of an ALJ for misconduct or failure to follow lawful agency directives or to perform his duties adequately. It should also clarify that the MSPB's review is limited to determining whether factual evidence exists to support the agency's proffered good faith grounds.[7]

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[7] The removal issue is fairly encompassed within the question presented whether the Commission's ALJs "are Officers of the United States within the meaning of the Appointments Clause." Pet. i. Just

A. The President's Constitutional Responsibility To Faithfully Execute The Laws Requires Adequate Authority To Remove Subordinate Officers

1. By vesting in the President "[t]he executive Power" of the United States, U.S. Const. Art. II, § 1, Cl. 1, and charging him with the duty to "take Care that the Laws be faithfully executed," *id.* § 3, Article II of the Constitution "confers on the President 'the general administrative control of those executing the laws.'" *Free Enter. Fund*, 561 U.S. at 492 (quoting *Myers* v. *United States*, 272 U.S. 52, 164 (1926)). The Framers understood the close connection between the President's ability to discharge his responsibilities as head of the Executive Branch and his control over its personnel. As James Madison explained, "if any power whatsoever is in its nature Executive, it is the power of appointing, overseeing, and controlling those who execute the laws." 1 Annals of Cong. 463 (1789) (Joseph Gales ed., 1834); see *Free Enter. Fund*, 561 U.S. at 501 (describing those powers as "perhaps *the* key means" through which the President may resist encroachment on executive power). The President's "ability to execute the laws" is thus inextricably linked to his authority to

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as a determination that ALJs are constitutional "Officers" has consequences under the Constitution for the manner of their appointment, so too does it implicate the procedures under which they may permissibly be removed from that office. See U.S. Cert. Br. 19-21. Should the Court agree that the Commission's ALJs are officers, therefore, the scope of the appropriate remedy in this case will depend on whether the Court concludes that the ALJ who presided over petitioners' hearing was subject to appointment and removal in conformance with constitutional constraints. See Cert. Reply Br. 11 (acknowledging that petitioners "would raise the removal issue," if not resolved here, as a defense in a further proceeding on remand before the Commission).

"hold[] his subordinates accountable for their conduct." *Free Enter. Fund*, 561 U.S. at 496.

The Constitution gives the President what the Framers saw as the "traditional" means of ensuring accountability: the "power to oversee executive officers through removal." *Free Enter. Fund*, 561 U.S. at 492. The power to remove, being "incident to the power of appointment," rests with the appointing authority absent an express statement to the contrary. *Ex parte Hennen*, 38 U.S. (13 Pet.) 230, 261 (1839). "[B]ecause that traditional executive power was not 'expressly taken away'" by the Constitution, "'it remained with the President'" in the first instance. *Free Enter. Fund*, 561 U.S. at 492 (quoting Letter from James Madison to Thomas Jefferson (June 30, 1789), 16 *Documentary History of the First Federal Congress* 893 (2004)). The President is accordingly authorized under our constitutional system to remove all principal officers, as well as all "inferior Officers" he has appointed. U.S. Const. Art. II, § 2, Cl. 2. Other "inferior Officers," whose appointments have been vested in "the Heads of Departments," may be removed by those Department Heads—who are themselves removable by the President. *Ibid.* As this Court has explained, "[o]nce an officer is appointed, it is only the authority that can remove him, and not the authority that appointed him, that he must fear and, in the performance of his functions, obey." *Bowsher* v. *Synar*, 478 U.S. 714, 726 (1986) (citation omitted).

Just as the President's "selection of administrative officers is essential to the execution of the laws by him, so must be his power of removing those for whom he can not continue to be responsible." *Myers*, 272 U.S. at 117. Absent adequate authority to remove his subordinates, the President could plausibly "escape responsibility for

his choices by pretending that they are not his own." *Free Enter. Fund*, 561 U.S. at 497. And if the Executive Branch itself were to "slip from the Executive's control," executive authority would similarly become unaccountable to the will of "the people." *Id.* at 499. The removal power thus is a key safeguard of democratic self-governance, preserving an unbroken chain of responsibility from the American people to the public officials who serve them. See 1 Annals of Cong. at 499 (Madison) ("[T]he lowest officers, the middle grade, and the highest, will depend, as they ought, on the President, and the President on the community.").

2. Consistent with these principles, this Court has countenanced only limited restrictions on the authority of the President to remove executive officers. As to principal officers, the Court has sustained such restrictions only with respect to members of certain multi-member independent agencies. See *Free Enter. Fund*, 561 U.S. at 493-494. As to inferior officers, this Court has twice upheld restrictions on removal authority. But neither decision provides justification for undercutting the fundamental constitutional requirement that the Executive have adequate means to supervise and instruct officers in the performance of their duties.

In *United States* v. *Perkins*, 116 U.S. 483 (1886), the Court held that the Secretary of the Navy could be required by statute, before removing a naval cadet-engineer during peacetime, to make a misconduct finding or convene a court-martial. *Id.* at 485. It was undisputed in *Perkins* that the cadet was discharged, not for any reason related to performance, but solely due to the want of a vacancy for him. *Id.* at 483. The Court thus had no cause to consider what sort of misconduct or performance-related justification would be adequate

to support removal under the terms of the statute. Cf. *Free Enter. Fund*, 561 U.S. at 507 ("Military officers are broadly subject to Presidential control through the chain of command and through the President's powers as Commander in Chief."). Thus, although *Perkins* addressed a statute that imposed some restrictions on the removal of certain military officers, it did not suggest that such officers could be placed beyond adequate Executive Branch supervision.

In *Morrison* v. *Olson*, 487 U.S. 654 (1988), the Court upheld a statute that allowed the Attorney General to remove an independent counsel only for "good cause." *Id.* at 685-693. The Court declined to decide "exactly what is encompassed within the term 'good cause,'" but stressed its understanding that "the Attorney General may remove an independent counsel for 'misconduct.'" *Id.* at 692 (quoting H.R. Conf. Rep. No. 452, 100th Cong., 1st Sess. 37 (1987)). Through that removal authority, the Court asserted, the President "retains ample authority to assure that the counsel is competently performing his or her statutory responsibilities." *Ibid.* The Court also emphasized that its conclusion rested in part on the independent counsel's "limited jurisdiction and tenure and lack[of] policymaking or significant administrative authority." *Id.* at 691. Although the independent counsel did exercise "discretion and judgment" in carrying out his responsibilities, the Court concluded that "the President's need to control the exercise of that discretion [was not] so central to the functioning of the Executive Branch as to require as a matter of constitutional law that the counsel be terminable at will by the President." *Id.* at 691-692.

3. The Court reached a different result in *Free Enterprise Fund*, where it struck down a statutory provision that imposed stringent limitations on the removal of inferior officers within an agency whose principal officers were themselves assumed to be subject to strict removal restrictions. Created by the Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745, the Public Company Accounting Oversight Board (PCAOB) was composed of five members appointed by the Commission. 561 U.S. at 484. The PCAOB's members enjoyed "rigorous" statutory removal protections: A member could be removed only upon a finding by the Commission—on the record and after a hearing—that the member "has willfully violated" the Sarbanes-Oxley Act, the securities laws, or the PCAOB's rules; "has willfully abused" his authority; or, "without reasonable justification or excuse," has failed to enforce compliance with the statutes, rules, or PCAOB standards. *Id.* at 486, 496 (quoting 15 U.S.C. 7217(d)(3)). And although no statute so provides, the parties in *Free Enterprise Fund* agreed (and this Court assumed) that the Commissioners themselves could be removed by the President only for "inefficiency, neglect of duty, or malfeasance in office." *Id.* at 487 (citation omitted).

This Court concluded, in light of the "novel" and "rigorous" barriers to removal that this two-tiered scheme created, that it left the President with insufficient ability to supervise the PCAOB's execution of the laws. *Free Enter. Fund*, 561 U.S. at 496. Each layer of tenure protection, the Court explained, significantly weakened executive control. The PCAOB's members were protected from removal by an "unusually high standard" that sharply constrained both the legal grounds for removal and the procedures under which it could occur;

even a member who committed a crime not specifically mentioned by the Sarbanes-Oxley Act (such as tax evasion) would be entitled to keep his position. *Id.* at 503. And the Commission's members, it was assumed, were themselves protected from removal absent conduct "so unreasonable as to constitute 'inefficiency, neglect of duty, or malfeasance in office.'" *Id.* at 496 (citation omitted). In combination, the Court explained, these "unusual protections from Presidential oversight" impermissibly undermined executive authority and political accountability. *Id.* at 506. Particularly in light of the PCAOB's important role as "the regulator of first resort and the primary law enforcement authority for a vital sector of our economy," the Court determined that the PCAOB's tenure protections were unconstitutional, and it invalidated and severed them from the rest of the statute. *Id.* at 508.

B. To Avoid Serious Constitutional Concerns, This Court Should Narrowly Construe "Good Cause" Restrictions On Removing ALJs

The APA provides that an ALJ may be removed by an agency head "only for good cause established and determined by the Merit Systems Protection Board," 5 U.S.C. 7521(a), whose members are themselves removable by the President "only for inefficiency, neglect of duty, or malfeasance in office," 5 U.S.C. 1202(d). Section 7521 is best interpreted to permit an agency to remove an ALJ for personal misconduct or for failure to follow lawful agency directives or to perform his duties adequately. The Court should construe the provision in that manner to safeguard the President's power to control and supervise the Executive Branch, while at the same time respecting the independence of ALJs in adjudicating individual cases. Although the Commission

(and some other agencies) have taken steps, following the government's filing of its response to the certiorari petition in this case, to ensure that future proceedings are overseen by properly appointed ALJs, see p. 3 n.2, *supra*, those proceedings will satisfy Article II only if the ALJs' removal protections also comply with constitutional constraints.

1. Congress did not define the term "good cause" or otherwise elaborate the permissible grounds on which an ALJ may be removed under Section 7521. The MSPB, in implementing Section 7521, has applied that term to a range of performance- and conduct-related justifications. The MSPB has recognized, *inter alia*, that removal may be appropriate where an ALJ "ignore[s] binding agency interpretations of law," *Social Sec. Admin.* v. *Anyel*, 58 M.S.P.R. 261, 269 (1993); that a "large proportion" of "significant" adjudicatory errors can constitute "good cause," *id.* at 265; and that, in unusual cases, an ALJ may be removed "on the basis of actions taken by him or her in the course of an adjudicatory proceeding," *In re Chocallo*, 1 M.S.P.R. 605, 610 (1980); see *ibid.* (permitting removal of ALJ for refusing to comply with an appellate agency order, declining to turn over records to agency officials when directed, and intemperate questioning of witnesses). The Constitution requires that an ALJ be removable on such grounds to enable the President and the agency head to ensure the soundness and integrity of the adjudicatory system for which they are responsible, and thus to ensure the faithful execution of the laws.

In other instances, however, the MSPB has declined to sustain the removal of ALJs even when misconduct has been substantiated by the agency seeking removal. The MSPB not only has "reserve[d] to itself the final

decision on [whether] good cause" for discipline exists, but also has asserted the right to determine "the appropriate penalty if it finds good cause." *Social Sec. Admin.* v. *Glover*, 23 M.S.P.R. 57, 64 (1984); see 5 C.F.R. 1201.140(b) (MSPB "will specify the penalty to be imposed"); see also, *e.g.*, *Social Sec. Admin.* v. *Brennan*, 27 M.S.P.R. 242, 248, 251 (1985), aff'd 787 F.2d 1559 (Fed. Cir.), cert. denied, 479 U.S. 985 (1986) (ALJ's pattern of "disruptive conduct," including refusal to follow office procedures, supported only a 60-day suspension rather than removal); *Glover*, 23 M.S.P.R. at 80 (ALJ's "intemperate" remarks to supervisor supported 120-day suspension without pay but not removal). The MSPB has similarly rejected, under certain circumstances, agency attempts to remove ALJs for deficient performance. Compare *Social Sec. Admin.* v. *Goodman*, 19 M.S.P.R. 321, 331 (1984) (ALJ could not be disciplined for productivity far below national averages in absence of specific evidence that ALJ's docket was comparable to those of peers), with *Shapiro* v. *Social Sec. Admin.*, 800 F.3d 1332, 1338 (Fed. Cir. 2015) (declining to follow *Goodman* and describing that decision as establishing "a virtually insurmountable burden of proof") (citation omitted).

Agency heads must be able to remove ALJs who refuse to follow agency policies and procedures, who frustrate the proper administration of adjudicatory proceedings, or who demonstrate deficient job performance. Otherwise, the agency head would be effectively in the same position as the Commission in *Free Enterprise Fund*: The agency head would "not [be] responsible for the [ALJ's] actions," and would instead be responsible only for deciding whether to initiate a removal action in light of the MSPB's standards. 561 U.S. at 496.

Without the authority to remove an ALJ for misconduct or for failure to follow lawful instructions or perform adequately, the President (and his chosen principal officers) cannot properly supervise those who exercise executive authority. "This violates the basic principle that the President cannot delegate ultimate responsibility or the active obligation to supervise that goes with it, because Article II makes a single President responsible for the actions of the Executive Branch." *Id.* at 496-497 (citation and internal quotation marks omitted).

These constitutional concerns are heightened in the context of independent agencies whose heads are themselves protected from removal by the President. If Section 7521 were construed not to allow the sort of removal authority described above, the additional level of tenure protection would only further undermine the President's ability to supervise the actions of the Executive Branch. See *Free Enter. Fund*, 561 U.S. at 496 ("Neither the President, nor anyone directly responsible to him, * * * has full control."). As a result, the President would be "stripped of the power [this Court's] precedents have preserved, and his ability to execute the laws—by holding his subordinates accountable for their conduct—[would be] impaired." *Ibid.*

2. To avoid these serious constitutional concerns, the Court should construe Section 7521 to permit agency heads to remove ALJs, subject to limited review by the MSPB, in a manner that is consistent with a constitutionally adequate level of Executive Branch supervision.

a. Section 7521(a) provides for the removal of ALJs for "good cause," which is most naturally read to authorize removal of an ALJ for misconduct, poor job performance, or failure to follow lawful directives. The

term "good cause," which is not otherwise defined by statute, was understood at the time of the APA's enactment to refer to a "[s]ubstantial" or "[l]egally sufficient ground or reason." *Black's Law Dictionary* 822 (4th ed. 1951). When specifically used to refer to employer actions such as the "discharg[e]" of personnel, the term's conventional meaning "include[d] any ground which is put forward by authorities in good faith and which is not arbitrary, irrational, unreasonable or irrelevant to the duties with which such authorities are charged." *Ibid.* (describing holding of *Nephew* v. *Willis*, 298 N.W. 376 (Mich. 1941)).

In adopting "good cause" to describe the standard for removing ALJs, Congress did not purport to deviate from that term's well-understood meaning. To the contrary, as the APA's co-sponsor explained, although "[t]he cause found must be real and demonstrable," and must be based on "facts and considerations warranting the finding," Congress had no intention to confine agencies to a limited category of acceptable reasons. S. Doc. No. 248, at 326 (Sen. McCarran). And although this Court has not previously attempted to provide a comprehensive definition of "good cause," it has rejected attempts to link that APA standard with another, more stringent standard drawn from a different context. See *Ramspeck*, 345 U.S. at 142 (rejecting argument that "good cause" for removing hearing examiners is the same as the showing required to remove Article III judges). The Court in *Ramspeck* explained that Congress did not intend for hearing examiners to be removed "at the whim or caprice of the agency or for political reasons," but that an agency is nevertheless authorized to discharge its hearing examiners for other, "legitimate reasons." *Id.* at 142-143.

The term "good cause" is thus best read to include an ALJ's failure to perform adequately or to follow agency policies, procedures, or instructions. See *Morrison*, 487 U.S. at 724 n.4 (Scalia, J., dissenting) (explaining that constitutionally permissible authority to remove an inferior officer "*for cause* * * * would include, of course, the failure to accept supervision"). This construction provides agencies with constitutionally sufficient latitude to remove an ALJ for appropriate job-related reasons; it ensures the agency head's control—and, by extension, the President's—over the important executive functions performed by these inferior officers. This construction, in addition to being the best reading of the text, is therefore supported by well-established principles of constitutional avoidance. See *Public Citizen* v. *Department of Justice*, 491 U.S. 440, 466 (1989).

Under the foregoing construction of the "for cause" standard, an ALJ would still be protected from removal for invidious reasons otherwise prohibited by law. See, *e.g.*, 42 U.S.C. 2000e-16(a) ("All personnel actions affecting employees * * * in executive agencies * * * shall be made free from any discrimination based on race, color, religion, sex, or national origin."). And the President, acting through his principal officers, would be restrained from removing an ALJ in order to influence the outcome in a particular adjudication. As this Court explained in *Myers*, "there may be duties of a quasi-judicial character imposed on executive officers and members of executive tribunals whose decisions after hearing affect interests of individuals, the discharge of which the President can not in a particular case properly influence or control." 272 U.S. at 135. But *Myers* also made clear that "even in such a case," the

President "may consider the decision after its rendition as a reason for removing the officer, on the ground that the discretion regularly entrusted to that officer by statute has not been on the whole intelligently or wisely exercised. Otherwise he does not discharge his own constitutional duty of seeing that the laws be faithfully executed." *Ibid.*

Although applying this construction of "good cause" to ALJs at independent agencies still results in a structure involving more than one layer of tenure protection, it comports with constitutional requirements. The intrusion on presidential authority is significantly less than under the provision invalidated in *Free Enterprise Fund*, in which the PCAOB's members could be removed only under an "unusually high standard" that required a "willful" violation of the law, a "willful" abuse of their authority, or an "unreasonable" failure to enforce legal requirements. 561 U.S. at 503. Under the natural interpretation of "good cause" and the standard advocated here, by contrast, an ALJ is removable for failure to accept lawful supervision or perform his duties adequately. ALJs could accordingly be held accountable, by the Heads of Departments and the President who appointed them, for failure to execute the laws faithfully. And even an independent agency head with sufficiently broad authority to remove an ALJ may be held accountable by the President for failing to exercise that authority appropriately. Construing "good cause" as the best reading of that term requires and we urge, therefore, effectively mitigates concerns with multiple

levels of removal protection, ensuring sufficient presidential control over the Executive Branch.[8]

b. In addition to adopting the construction of "good cause" described above, the Court should construe the statutory requirement that such cause be "established and determined by the Merit Systems Protection Board," 5 U.S.C. 7521(a), to ensure adequate supervision and accountability by the head of the agency whose laws, policies, and procedures the ALJ must follow. Doing so requires proper regard for the judgment of the head of the agency concerning what is required from subordinates in order to properly exercise the authority vested by law in the agency.

To accomplish that end, Section 7521 can reasonably be interpreted to mean that the cause relied upon by the agency for removing its ALJ has been *found by* the MSPB—that is, the MSPB has determined that factual evidence exists to support the agency's proffered, good-faith grounds. That construction differs from the MSPB's current practice of determining not simply whether facts exist to support the agency's determination, but whether in the MSPB's view those facts amount to "good cause" and also warrant removal or other sanctions sought by the agency. See *Glover*, 23 M.S.P.R. at 64. Reading the phrase "established and determined by the [MSPB]" in the manner proposed

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[8] *Free Enterprise Fund* was decided on the understanding that the Commission's members could not be removed from office by the President except for "inefficiency, neglect of duty, or malfeasance in office." 561 U.S. at 487 (citation omitted). We take no position here on whether such protections validly exist as a statutory or constitutional matter. It is also unnecessary for the Court to address those questions. The interpretation of "good cause" that is proposed here conforms to constitutional constraints even when the Department Head is permissibly insulated from presidential removal at will.

here is well within the range of constructions available to the Court under the canon of constitutional avoidance. See *Ramspeck*, 345 U.S. at 142 (APA "leaves with the agency the responsibility" to determine whether unneeded hearing examiners should be discharged, subject to appeal to Civil Service Commission to "prevent any devious practice by an agency which would abuse" that power). And thus interpreted, Section 7521 leaves agency heads with constitutionally adequate authority to ensure that ALJs are faithfully executing the law.

c. If the Court concludes that the interpretation of Section 7521 advocated here cannot be reconciled with the statute, then the limitations that the provision imposes on removal of the Commission's ALJs would be unconstitutional. To resolve those concerns, the Court should invalidate and sever only the portion or portions of Section 7521 that cannot be interpreted, under principles of constitutional avoidance, to accord agency heads appropriate supervision of ALJs as inferior officers within their agencies. Absent those unconstitutional requirements, the remaining statute would be "fully operative as a law," and "nothing in the statute's text or historical context makes it evident that Congress, faced with the limitations imposed by the Constitution, would have preferred" invalidation of the APA *in toto*. *Free Enter. Fund*, 561 U.S. at 509 (citation and internal quotation marks omitted).

3. In addition to articulating a standard under which ALJs may be removed from office, Section 7521 addresses the sequence of events that must occur before removal. It provides that "[a]n action may be taken against an [ALJ]" by the agency "only for good cause established and determined by the [MSPB] on the record *after opportunity for hearing before the Board*."

5 U.S.C. 7521(a) (emphasis added); see 5 U.S.C. 7521(b) (identifying "removal" as an "action" covered by subsection (a)). Removal thus may occur only "after" an MSPB hearing regarding good cause. As a result, an ALJ may remain in office—despite the employing agency's determination that the ALJ's misconduct or poor performance warrants removal—until the MSPB has ruled on the dispute. That required sequence for ALJs differs from the rules that apply to most federal employees, who may be removed from the civil service promptly, subject to minimal procedural requirements (including at least 30 days' notice and 7 days to respond). See 5 U.S.C. 7513(b); see also 5 U.S.C. 7701(b)(2) (employee's removal remains in effect until agency's removal decision is overturned by MSPB).

The procedures under Section 7521 for removing ALJs may, in some circumstances, undermine the ability of Department Heads to properly supervise their subordinates in the manner the Constitution requires. An agency's decision to remove an ALJ may be a determination that the ALJ cannot be trusted to faithfully execute the laws. Yet the ALJ's removal from office cannot be effectuated until the MSPB rules, which may take a substantial period of time—in some cases, years. See, *e.g.*, *Social Sec. Admin.* v. *Boini*, 123 M.S.P.R. 302 (2016) (Tbl.) (MSPB ruling 44 months after agency sought to remove ALJ); *Social Sec. Admin.* v. *Long*, 113 M.S.P.R. 190 (2010), aff'd, 635 F.3d 526 (Fed. Cir. 2011) (19 months). In the interim, the ALJ will continue to occupy the office for which the agency has deemed him unfit, and he will continue to draw a salary from the agency.

This case, however, does not implicate those constitutional concerns. Agencies currently possess the authority to reassign responsibilities away from ALJs while awaiting MSPB review of a removal decision. See *Mahoney* v. *Donovan*, 721 F.3d 633, 637 (D.C. Cir. 2013), cert. denied, 134 S. Ct. 2724 (2014). That authority avoids the possibility that an ALJ might continue to adjudicate cases beyond the point at which the Department Head has lost confidence in the ALJ's ability to exercise appropriate judgment. Other concerns with an ALJ's compensation or continued employment within the agency (albeit without his duties) do not bear on a private litigant's constitutional right to an adjudication before a properly appointed decision-maker. See *Printz* v. *United States*, 521 U.S. 898, 935 (1997) (declining, in context of federalism-based constitutional claim, to address validity of provisions implicating "rights and obligations of parties not before the Court"). Such concerns bear only on the Executive Branch's ability to adequately supervise ALJs, and thus should be addressed in appropriate cases between employing agencies and their ALJs.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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APPENDIX

1. Article II, Section 2, Clause 2 of the United States Constitution provides in relevant part:

> * * * [H]e shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

2. 5 U.S.C. 556 provides:

> **Hearings; presiding employees; powers and duties; burden of proof; evidence; record as basis of decision**
>
> (a) This section applies, according to the provisions thereof, to hearings required by section 553 or 554 of this title to be conducted in accordance with this section.
>
> (b) There shall preside at the taking of evidence—
>
> (1) the agency;
>
> (2) one or more members of the body which comprises the agency; or
>
> (3) one or more administrative law judges appointed under section 3105 of this title.
>
> This subchapter does not supersede the conduct of specified classes of proceedings, in whole or in part, by or before boards or other employees specially provided for

by or designated under statute. The functions of presiding employees and of employees participating in decisions in accordance with section 557 of this title shall be conducted in an impartial manner. A presiding or participating employee may at any time disqualify himself. On the filing in good faith of a timely and sufficient affidavit of personal bias or other disqualification of a presiding or participating employee, the agency shall determine the matter as a part of the record and decision in the case.

(c) Subject to published rules of the agency and within its powers, employees presiding at hearings may—

(1) administer oaths and affirmations;

(2) issue subpenas authorized by law;

(3) rule on offers of proof and receive relevant evidence;

(4) take depositions or have depositions taken when the ends of justice would be served;

(5) regulate the course of the hearing;

(6) hold conferences for the settlement or simplification of the issues by consent of the parties or by the use of alternative means of dispute resolution as provided in subchapter IV of this chapter;

(7) inform the parties as to the availability of one or more alternative means of dispute resolution, and encourage use of such methods;

(8) require the attendance at any conference held pursuant to paragraph (6) of at least one representative of each party who has authority to negotiate concerning resolution of issues in controversy;

(9) dispose of procedural requests or similar matters;

(10) make or recommend decisions in accordance with section 557 of this title; and

(11) take other action authorized by agency rule consistent with this subchapter.

(d) Except as otherwise provided by statute, the proponent of a rule or order has the burden of proof. Any oral or documentary evidence may be received, but the agency as a matter of policy shall provide for the exclusion of irrelevant, immaterial, or unduly repetitious evidence. A sanction may not be imposed or rule or order issued except on consideration of the whole record or those parts thereof cited by a party and supported by and in accordance with the reliable, probative, and substantial evidence. The agency may, to the extent consistent with the interests of justice and the policy of the underlying statutes administered by the agency, consider a violation of section 557(d) of this title sufficient grounds for a decision adverse to a party who has knowingly committed such violation or knowingly caused such violation to occur. A party is entitled to present his case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts. In rule making or determining claims for money or benefits or applications for initial licenses an agency may, when a party will not be prejudiced thereby, adopt procedures for the submission of all or part of the evidence in written form.

(e) The transcript of testimony and exhibits, together with all papers and requests filed in the proceeding,

constitutes the exclusive record for decision in accordance with section 557 of this title and, on payment of lawfully prescribed costs, shall be made available to the parties. When an agency decision rests on official notice of a material fact not appearing in the evidence in the record, a party is entitled, on timely request, to an opportunity to show the contrary.

3. 5 U.S.C. 557 provides:

Initial decisions; conclusiveness; review by agency; submissions by parties; contents of decisions; record

(a) This section applies, according to the provisions thereof, when a hearing is required to be conducted in accordance with section 556 of this title.

(b) When the agency did not preside at the reception of the evidence, the presiding employee or, in cases not subject to section 554(d) of this title, an employee qualified to preside at hearings pursuant to section 556 of this title, shall initially decide the case unless the agency requires, either in specific cases or by general rule, the entire record to be certified to it for decision. When the presiding employee makes an initial decision, that decision then becomes the decision of the agency without further proceedings unless there is an appeal to, or review on motion of, the agency within time provided by rule. On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision except as it may limit the issues on notice or by rule. When the agency makes the decision without having presided at the reception of the evidence, the presiding employee or an employee qualified to preside at hearings pursuant to section 556 of this

title shall first recommend a decision, except that in rule making or determining applications for initial licenses—

(1) instead thereof the agency may issue a tentative decision or one of its responsible employees may recommend a decision; or

(2) this procedure may be omitted in a case in which the agency finds on the record that due and timely execution of its functions imperatively and unavoidably so requires.

(c) Before a recommended, initial, or tentative decision, or a decision on agency review of the decision of subordinate employees, the parties are entitled to a reasonable opportunity to submit for the consideration of the employees participating in the decisions—

(1) proposed findings and conclusions; or

(2) exceptions to the decisions or recommended decisions of subordinate employees or to tentative agency decisions; and

(3) supporting reasons for the exceptions or proposed findings or conclusions.

The record shall show the ruling on each finding, conclusion, or exception presented. All decisions, including initial, recommended, and tentative decisions, are a part of the record and shall include a statement of—

(A) findings and conclusions, and the reasons or basis therefor, on all the material issues of fact, law, or discretion presented on the record; and

(B) the appropriate rule, order, sanction, relief, or denial thereof.

(d)(1) In any agency proceeding which is subject to subsection (a) of this section, except to the extent required for the disposition of ex parte matters as authorized by law—

(A) no interested person outside the agency shall make or knowingly cause to be made to any member of the body comprising the agency, administrative law judge, or other employee who is or may reasonably be expected to be involved in the decisional process of the proceeding, an ex parte communication relevant to the merits of the proceeding;

(B) no member of the body comprising the agency, administrative law judge, or other employee who is or may reasonably be expected to be involved in the decisional process of the proceeding, shall make or knowingly cause to be made to any interested person outside the agency an ex parte communication relevant to the merits of the proceeding;

(C) a member of the body comprising the agency, administrative law judge, or other employee who is or may reasonably be expected to be involved in the decisional process of such proceeding who receives, or who makes or knowingly causes to be made, a communication prohibited by this subsection shall place on the public record of the proceeding:

(i) all such written communications;

(ii) memoranda stating the substance of all such oral communications; and

(iii) all written responses, and memoranda stating the substance of all oral responses, to the materials described in clauses (i) and (ii) of this subparagraph;

(D) upon receipt of a communication knowingly made or knowingly caused to be made by a party in violation of this subsection, the agency, administrative law judge, or other employee presiding at the hearing may, to the extent consistent with the interests of justice and the policy of the underlying statutes, require the party to show cause why his claim or interest in the proceeding should not be dismissed, denied, disregarded, or otherwise adversely affected on account of such violation; and

(E) the prohibitions of this subsection shall apply beginning at such time as the agency may designate, but in no case shall they begin to apply later than the time at which a proceeding is noticed for hearing unless the person responsible for the communication has knowledge that it will be noticed, in which case the prohibitions shall apply beginning at the time of his acquisition of such knowledge.

(2) This subsection does not constitute authority to withhold information from Congress.

4. 5 U.S.C. 3105 provides:

Appointment of administrative law judges

Each agency shall appoint as many administrative law judges as are necessary for proceedings required to be conducted in accordance with sections 556 and 557 of this title. Administrative law judges shall be assigned to cases in rotation so far as practicable, and may not perform duties inconsistent with their duties and responsibilities as administrative law judges.

5. 5 U.S.C. 7521 provides:

Actions against administrative law judges

(a) An action may be taken against an administrative law judge appointed under section 3105 of this title by the agency in which the administrative law judge is employed only for good cause established and determined by the Merit Systems Protection Board on the record after opportunity for hearing before the Board.

(b) The actions covered by this section are—

(1) a removal;

(2) a suspension;

(3) a reduction in grade;

(4) a reduction in pay; and

(5) a furlough of 30 days or less;

but do not include—

(A) a suspension or removal under section 7532 of this title;

(B) a reduction-in-force action under section 3502 of this title; or

(C) any action initiated under section 1215 of this title.

6. 15 U.S.C. 78d-1 provides:

Delegation of functions by Commission

(a) Authorization; functions delegable; eligible persons; application of other laws

In addition to its existing authority, the Securities and Exchange Commission shall have the authority to delegate, by published order or rule, any of its functions to a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee board, including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter. Nothing in this section shall be deemed to supersede the provisions of section 556(b) of title 5, or to authorize the delegation of the function of rulemaking as defined in subchapter II of chapter 5 of title 5, with reference to general rules as distinguished from rules of particular applicability, or of the making of any rule pursuant to section 78s(c) of this title.

(b) Right of review; procedure

With respect to the delegation of any of its functions, as provided in subsection (a) of this section, the Commission shall retain a discretionary right to review the action of any such division of the Commission, individual Commissioner, administrative law judge, employee, or employee board, upon its own initiative or upon petition of a party to or intervenor in such action, within such time and in such manner as the Commission by rule shall prescribe. The vote of one member of the Commission shall be sufficient to bring any such action before the Commission for review. A person or party shall be entitled to review by the Commission if he or it is adversely

affected by action at a delegated level which (1) denies any request for action pursuant to section 77h(a) or section 77h(c) of this title or the first sentence of section 781(d) of this title; (2) suspends trading in a security pursuant to section 781(k) of this title; or (3) is pursuant to any provision of this chapter in a case of adjudication, as defined in section 551 of title 5, not required by this chapter to be determined on the record after notice and opportunity for hearing (except to the extent there is involved a matter described in section 554(a)(1) through (6) of such title 5).

(c) Finality of delegated action

If the right to exercise such review is declined, or if no such review is sought within the time stated in the rules promulgated by the Commission, then the action of any such division of the Commission, individual Commissioner, administrative law judge, employee, or employee board, shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission.

7. 17 C.F.R. 201.110 provides:

Presiding officer.

All proceedings shall be presided over by the Commission or, if the Commission so orders, by a hearing officer. When the Commission designates that the hearing officer shall be an administrative law judge, the Chief Administrative Law Judge shall select, pursuant to 17 CFR 200.30-10, the administrative law judge to preside.

8. 17 C.F.R. 201.111 provides:

Hearing officer: Authority.

The hearing officer shall have the authority to do all things necessary and appropriate to discharge his or her duties. No provision of these Rules of Practice shall be construed to limit the powers of the hearing officer provided by the Administrative Procedure Act, 5 U.S.C. 556, 557. The powers of the hearing officer include, but are not limited to, the following:

(a) Administering oaths and affirmations;

(b) Issuing subpoenas authorized by law and revoking, quashing, or modifying any such subpoena;

(c) Receiving relevant evidence and ruling upon the admission of evidence and offers of proof;

(d) Regulating the course of a proceeding and the conduct of the parties and their counsel;

(e) Holding prehearing and other conferences as set forth in § 201.221 and requiring the attendance at any such conference of at least one representative of each party who has authority to negotiate concerning the resolution of issues in controversy;

(f) Recusing himself or herself upon motion made by a party or upon his or her own motion;

(g) Ordering, in his or her discretion, in a proceeding involving more than one respondent, that the interested division indicate, on the record, at least one day prior to the presentation of any evidence, each respondent against whom that evidence will be offered;

(h) Subject to any limitations set forth elsewhere in these Rules of Practice, considering and ruling upon all

procedural and other motions, including a motion to correct a manifest error of fact in the initial decision. A motion to correct is properly filed under this Rule only if the basis for the motion is a patent misstatement of fact in the initial decision. Any motion to correct must be filed within ten days of the initial decision. A brief in opposition may be filed within five days of a motion to correct. The hearing officer shall have 20 days from the date of filing of any brief in opposition filed to rule on a motion to correct;

(i) Preparing an initial decision as provided in § 201.360;

(j) Upon notice to all parties, reopening any hearing prior to the filing of an initial decision therein, or, if no initial decision is to be filed, prior to the time fixed for the filing of final briefs with the Commission; and

(k) Informing the parties as to the availability of one or more alternative means of dispute resolution, and encouraging the use of such methods.

9. 17 C.F.R. 201.180 provides:

Sanctions.

(a) *Contemptuous conduct*—(1) *Subject to exclusion or suspension.* Contemptuous conduct by any person before the Commission or a hearing officer during any proceeding, including at or in connection with any conference, deposition or hearing, shall be grounds for the Commission or the hearing officer to:

(i) Exclude that person from such deposition, hearing or conference, or any portion thereof; and/or

(ii) Summarily suspend that person from representing others in the proceeding in which such conduct occurred for the duration, or any portion, of the proceeding.

(2) *Review procedure.* A person excluded from a deposition, hearing or conference, or a counsel summarily suspended from practice for the duration or any portion of a proceeding, may seek review of the exclusion or suspension by filing with the Commission, within three days of the exclusion or suspension order, a motion to vacate the order. The Commission shall consider such motion on an expedited basis as provided in § 201.500.

(3) *Adjournment.* Upon motion by a party represented by counsel subject to an order of exclusion or suspension, an adjournment shall be granted to allow the retention of new counsel. In determining the length of an adjournment, the Commission or hearing officer shall consider, in addition to the factors set forth in § 201.161, the availability of co-counsel for the party or of other members of a suspended counsel's firm.

(b) *Deficient filings; leave to cure deficiencies.* The Commission or the hearing officer may reject, in whole or in part, any filing that fails to comply with any requirements of these Rules of Practice or of any order issued in the proceeding in which the filing was made. Any such filings shall not be part of the record. The Commission or the hearing officer may direct a party to cure any deficiencies and to resubmit the filing within a fixed time period.

(c) *Failure to make required filing or to cure deficient filing.* The Commission or the hearing officer may enter a default pursuant to § 201.155, dismiss one or

more claims, decide the particular claim(s) at issue against that person, or prohibit the introduction of evidence or exclude testimony concerning that claim if a person fails:

(1) To make a filing required under these Rules of Practice; or

(2) To cure a deficient filing within the time specified by the Commission or the hearing officer pursuant to paragraph (b) of this section.

10. 17 C.F.R. 201.360 provides:

Initial decision of hearing officer and timing of hearing.

(a)(1) *When required.* Unless the Commission directs otherwise, the hearing officer shall prepare an initial decision in any proceeding in which the Commission directs a hearing officer to preside at a hearing, provided, however, that an initial decision may be waived by the parties with the consent of the hearing officer pursuant to § 201.202.

(2) *Time period for filing initial decision and for hearing*—(i) *Initial decision.* In the order instituting proceedings, the Commission will specify a time period in which the hearing officer's initial decision must be filed with the Secretary. In the Commission's discretion, after consideration of the nature, complexity, and urgency of the subject matter, and with due regard for the public interest and the protection of investors, this time period will be either 30, 75, or 120 days. The time period will run from the occurrence of the following events:

(A) The completion of post-hearing briefing in a proceeding where the hearing has been completed; or

(B) The completion of briefing on a § 201.250 motion in the event the hearing officer has determined that no hearing is necessary; or

(C) The determination by the hearing officer that, pursuant to § 201.155, a party is deemed to be in default and no hearing is necessary.

(ii) *Hearing.* Under the 120-day timeline, the hearing officer shall issue an order scheduling the hearing to begin approximately four months (but no more than ten months) from the date of service of the order instituting the proceeding. Under the 75-day timeline, the hearing officer shall issue an order scheduling the hearing to begin approximately 2½ months (but no more than six months) from the date of service of the order instituting the proceeding. Under the 30-day timeline, the hearing officer shall issue an order scheduling the hearing to begin approximately one month (but no more than four months) from the date of service of the order instituting the proceeding. These deadlines confer no substantive rights on respondents. If a stay is granted pursuant to § 201.161(c)(2)(i) or § 201.210(c)(3), the time period specified in the order instituting proceedings in which the hearing officer's initial decision must be filed with the Secretary, as well as any other time limits established in orders issued by the hearing officer in the proceeding, shall be automatically tolled during the period while the stay is in effect.

(3) *Certification of extension; motion for extension.* (i) In the event that the hearing officer presiding over the proceeding determines that it will not be possible to

file the initial decision within the specified period of time, the hearing officer may certify to the Commission in writing the need to extend the initial decision deadline by up to 30 days for case management purposes. The certification must be issued no later than 30 days prior to the expiration of the time specified for the issuance of an initial decision and be served on the Commission and all parties in the proceeding. If the Commission has not issued an order to the contrary within 14 days after receiving the certification, the extension set forth in the hearing officer's certification shall take effect.

(ii) Either in addition to a certification of extension, or instead of a certification of extension, the Chief Administrative Law Judge may submit a motion to the Commission requesting an extension of the time period for filing the initial decision. First, the hearing officer presiding over the proceeding must consult with the Chief Administrative Law Judge. Following such consultation, the Chief Administrative Law Judge may determine, in his or her discretion, to submit a motion to the Commission requesting an extension of the time period for filing the initial decision. This motion may request an extension of any length but must be filed no later than 15 days prior to the expiration of the time specified in the certification of extension, or if there is no certification of extension, 30 days prior to the expiration of the time specified in the order instituting proceedings. The motion will be served upon all parties in the proceeding, who may file with the Commission statements in support of or in opposition to the motion. If the Commission determines that additional time is necessary or appropriate in the public interest, the Commission shall issue an order extending the time period for filing the initial decision.

(iii) The provisions of this paragraph (a)(3) confer no rights on respondents.

(b) *Content.* An initial decision shall include findings and conclusions, and the reasons or basis therefor, as to all the material issues of fact, law or discretion presented on the record and the appropriate order, sanction, relief, or denial thereof. The initial decision shall also state the time period, not to exceed 21 days after service of the decision, except for good cause shown, within which a petition for review of the initial decision may be filed. The reasons for any extension of time shall be stated in the initial decision. The initial decision shall also include a statement that, as provided in paragraph (d) of this section:

(1) The Commission will enter an order of finality as to each party unless a party or an aggrieved person entitled to review timely files a petition for review of the initial decision or a motion to correct a manifest error of fact in the initial decision with the hearing officer, or the Commission determines on its own initiative to review the initial decision; and

(2) If a party or an aggrieved person entitled to review timely files a petition for review or a motion to correct a manifest error of fact in the initial decision with the hearing officer, or if the Commission takes action to review as to a party or an aggrieved person entitled to review, the initial decision shall not become final as to that party or person.

(c) *Filing, service and publication.* The Secretary shall promptly serve the initial decision upon the parties and shall promptly publish notice of the filing thereof on

the SEC Web site. Thereafter, the Secretary shall publish the initial decision in the SEC Docket; provided, however, that in nonpublic proceedings no notice shall be published unless the Commission otherwise directs.

(d) *Finality.* (1) If a party or an aggrieved person entitled to review timely files a petition for review or a motion to correct a manifest error of fact in the initial decision, or if the Commission on its own initiative orders review of a decision with respect to a party or a person aggrieved who would be entitled to review, the initial decision shall not become final as to that party or person.

(2) If a party or aggrieved person entitled to review fails to file timely a petition for review or a motion to correct a manifest error of fact in the initial decision, and if the Commission does not order review of a decision on its own initiative, the Commission will issue an order that the decision has become final as to that party. The decision becomes final upon issuance of the order. The order of finality shall state the date on which sanctions, if any, take effect. Notice of the order shall be published in the *SEC Docket* and on the SEC Web site.

11. 17 C.F.R. 201.411 provides:

Commission consideration of initial decisions by hearing officers.

(a) *Scope of review.* The Commission may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part, an initial decision by a hearing officer and may make any findings or conclusions that in its judgment are proper and on the basis of the record.

(b) *Standards for granting review pursuant to a petition for review*—(1) *Mandatory review.* After a petition for review has been filed, the Commission shall review any initial decision that:

(i) Denies any request for action pursuant to Section 8(a) or Section 8(c) of the Securities Act of 1933, 15 U.S.C. 77h(a), (c), or the first sentence of Section 12(d) of the Exchange Act, 15 U.S.C. 781(d);

(ii) Suspends trading in a security pursuant to Section 12(k) of the Exchange Act, 15 U.S.C. 781(k); or

(iii) Is in a case of adjudication (as defined in 5 U.S.C. 551) not required to be determined on the record after notice and opportunity for hearing (except to the extent there is involved a matter described in 5 U.S.C. 554(a)(1) through (6)).

(2) *Discretionary review.* The Commission may decline to review any other decision. In determining whether to grant review, the Commission shall consider whether the petition for review makes a reasonable showing that:

(i) A prejudicial error was committed in the conduct of the proceeding; or

(ii) The decision embodies:

(A) A finding or conclusion of material fact that is clearly erroneous; or

(B) A conclusion of law that is erroneous; or

(C) An exercise of discretion or decision of law or policy that is important and that the Commission should review.

(c) *Commission review other than pursuant to a petition for review.* The Commission may, on its own initiative, order review of any initial decision, or any portion of any initial decision, within 21 days after the end of the period established for filing a petition for review pursuant to § 201.410(b). A party who does not intend to file a petition for review, and who desires the Commission's determination whether to order review on its own initiative to be made in a shorter time, may make a motion for an expedited decision, accompanied by a written statement that the party waives its right to file a petition for review. The vote of one member of the Commission, conveyed to the Secretary, shall be sufficient to bring a matter before the Commission for review.

(d) *Limitations on matters reviewed.* Review by the Commission of an initial decision shall be limited to the issues specified in an opening brief that complies with § 201.450(b), or the issues, if any, specified in the briefing schedule order issued pursuant to § 201.450(a). Any exception to an initial decision not supported in an opening brief that complies with § 201.450(b) may, at the discretion of the Commission, be deemed to have been waived by the petitioner. On notice to all parties, however, the Commission may, at any time prior to issuance of its decision, raise and determine any other matters that it deems material, with opportunity for oral or written argument thereon by the parties.

(e) *Summary affirmance.* (1) At any time within 21 days after the filing of a petition for review pursuant to § 201.410(b), any party may file a motion in accordance with § 201.154 asking that the Commission summarily affirm an initial decision. Any party may file an opposition and reply to such motion in accordance with

§ 201.154. Pending determination of the motion for summary affirmance, the Commission, in its discretion, may delay issuance of a briefing schedule order pursuant to § 201.450.

(2) Upon consideration of the motion and any opposition or upon its own initiative, the Commission may summarily affirm an initial decision. The Commission may grant summary affirmance if it finds that no issue raised in the initial decision warrants consideration by the Commission of further oral or written argument. The Commission will decline to grant summary affirmance upon a reasonable showing that a prejudicial error was committed in the conduct of the proceeding or that the decision embodies an exercise of discretion or decision of law or policy that is important and that the Commission should review.

(f) *Failure to obtain a majority.* In the event a majority of participating Commissioners do not agree to a disposition on the merits, the initial decision shall be of no effect, and an order will be issued in accordance with this result.

No. 17-130

IN THE
Supreme Court of the United States

RAYMOND J. LUCIA
AND RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ Of Certiorari
To The United States Court Of Appeals
For The District Of Columbia Circuit

REPLY BRIEF FOR PETITIONERS

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RULE 29.6 STATEMENT

The corporate disclosure statement contained in the Brief for Petitioners remains accurate.

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REPLY BRIEF FOR PETITIONERS

I. SEC ALJs Are Officers Of The United States

This Court has long recognized that "exercising significant authority" is the touchstone for whether a federal official is an Officer of the United States within the meaning of the Appointments Clause. *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam). SEC ALJs readily satisfy that standard. *See* Pet. Br. 20-26; U.S. Br. 20-32. In defending the judgment (but not the reasoning) of the court below, the Court-appointed *Amicus* therefore proposes rewriting the intentionally flexible *Buckley* standard to include a rigid two-part test under which all Officers must have *both* final decision-making authority *and* the power to exercise that authority in their own name, without any approval by a superior. *Amicus* does not, however, argue that *Buckley* was "wrongly decided," nor does he offer any "'special justification'" for "overturning [such] a long-settled precedent." *Halliburton Co.* v. *Erica P. John Fund, Inc.*, 134 S. Ct. 2398, 2407 (2014) (citation omitted). *Amicus* has not made the case for the radical reworking of *Buckley* that his proposed approach would entail.

A. SEC ALJs Are Officers Under The *Buckley* Standard

The Court has consistently and without apparent difficulty applied *Buckley*'s standard to conclude that non-Article III adjudicators who preside over adversarial proceedings are Officers, *Freytag* v. *Comm'r*, 501 U.S. 868, 881-82 (1991), whether or not they can render final decisions, *Edmond* v. *United States*, 520 U.S. 651, 652 (1997). Under those precedents,

SEC ALJs are Officers—full stop. Pet. Br. 20-26; U.S. Br. 20-32.

1. As *Buckley* recognized, the term "Officer" was "taken by all concerned" at the Founding "to embrace all appointed officials exercising responsibility" under federal law. 424 U.S. at 131. That broad definition served the Appointments Clause's purpose of ensuring "political accountability relative to important Government assignments." *Edmond*, 520 U.S. at 663. Accordingly, a long line of precedents has held that quasi-judicial officials as varied as court commissioners, *Go-Bart Importing Co.* v. *United States*, 282 U.S. 344, 352-54 (1931), district-court clerks, *Ex parte Hennen*, 38 U.S. (13 Pet.) 230, 258 (1839), and judges of election, *Ex parte Siebold*, 100 U.S. 371, 397-99 (1880), are Officers.

Distilling these principles and precedents, *Buckley* articulated a framework for determining Officer status: Those who exercise "significant" federal authority are Officers, whereas "lesser functionaries subordinate to officers of the United States" are not. 424 U.S. at 126 & n.162 (citing *Auffmordt* v. *Hedden*, 137 U.S. 310, 327 (1890)). This framework is necessarily context-dependent—considerations relevant to an adjudicator's status, for instance, may differ from those relevant to an administrator's. The Court has repeatedly reiterated *Buckley*'s "significant authority" standard, expressing no doubts about its utility or vitality. *See Free Enter. Fund* v. *PCAOB*, 561 U.S. 477, 506 (2010); *see also NLRB* v. *SW Gen., Inc.*, 137 S. Ct. 929, 947 (2017) (Thomas, J., concurring).

Although *Amicus* complains (at 28) that *Buckley*'s standard has not been "fleshed out," *Buckley*'s discussion of the Appointments Clause was extensive, and the Court has since applied *Buckley* in a series of cases

involving, as here, non-Article III adjudicators. Each time, the Court unanimously held that adjudicators who preside over adversarial enforcement proceedings are Officers—most notably, that special trial judges (STJs) of the Tax Court are Officers because they exercise significant authority in presiding over hearings and shaping the record. *Freytag*, 501 U.S. at 881-82; *see also Edmond*, 520 U.S. at 662, 665 (military appellate judges whose decisions are subject to review are Officers); *Weiss* v. *United States*, 510 U.S. 163, 167-69 (1994) (military trial judges whose sentences are never final are Officers). This Court has *never* held that an adjudicatory official is *not* an Officer.

2. SEC ALJs undisputedly exercise federal authority; and that authority is "significant" because it includes all the functions this Court found "significant" in *Freytag*—"tak[ing] testimony, conduct[ing] trials, rul[ing] on the admissibility of evidence, and hav[ing] the power to enforce compliance with discovery orders," 501 U.S. at 881-82—and then some. Among other things, SEC ALJs:

- take testimony by "[e]xamin[ing] witnesses," 17 C.F.R. § 200.14(a)(4), and regulating cross-examination, *id.* § 201.326;
- conduct trials by "[r]egulat[ing] the course of hearing[s]," *id.* §§ 200.14(a)(5), 201.111(d);
- receive "relevant evidence" and rule upon its admissibility, *id.* § 201.111(c);
- regulate discovery by "[i]ssu[ing] subpoenas," *id.* §§ 200.14(a)(2), 201.111(b), ordering depositions, *id.* §§ 201.233-.234, and ordering production of evidence, *id.* §§ 201.111(c), .230, .232; and

- enforce compliance with those orders by rejecting filings, *id.* § 201.180(b), and imposing sanctions for "contemptuous conduct," *id.* § 201.180(a).

Amicus never meaningfully addresses these powers, or the many others that Congress and the Commission have delegated to SEC ALJs. *See* Pet. Br. 21-23 (listing powers); U.S. Br. 21 (same). That lacuna is telling.

3. It is not seriously debatable that SEC ALJs are equivalent to STJs in every respect specified in *Freytag*. Indeed, *Amicus* reluctantly concedes (at 16) that "the Court might have viewed the hearing-related functions ... as by themselves sufficient to make [STJs] constitutional officers, even absent the ability to enter final binding judgments." His arguments that *Freytag* is nevertheless distinguishable are either illusory or irrelevant.

a. *Amicus* argues (at 46) that, unlike STJs, SEC ALJs cannot enter binding decisions in any category of cases. That is incorrect.

As the Commission has explained, SEC ALJs "have long exercised the authority to enter default orders that make findings, order payment of penalties and disgorgement, and order a party to cease and desist. And we have long understood such orders to be enforceable." *In re Alchemy Ventures, Inc.*, Exchange Act Release No. 70,708, 2013 WL 6173809, at *4 (Oct. 17, 2013). Although the Commission currently prefers its ALJs to enter initial decisions of default, *ibid.*, they indisputably have the *power* to enter immediately enforceable default decisions. *See* Pet. Br. 32; U.S. Br. 22 n.5.

Moreover, SEC ALJs enter initial decisions that are "deemed the action of the Commission" and become binding absent review. 15 U.S.C. § 78d-1(c); *see also* 17 C.F.R. § 201.360(d)(2). *Amicus* argues (at 47) that this statute "does not apply to ALJ initial decisions" because the Commission has not delegated final decision-making authority to ALJs. That question-begging argument cannot be reconciled with either the statute or the government's explanation of it. *See* U.S. Br. 35. And since *Congress* has permitted SEC ALJs to make final decisions, it does not matter for constitutional purposes whether the Commission has allowed them to exercise that power in any or every case.

Amicus also suggests (at 46) that the Commission "sanction[s]" each unreviewed decision. But if the Commission does not timely order review, it *must* enter a finality order. 5 U.S.C. § 557(b) ("initial decision[s]" become final "without further proceedings" absent further review). Moreover, SEC "staff"—not the Commission itself—"reviews *every* initial ALJ decision." Commissioner Robert J. Jackson, Jr., *Fact and Fiction: The SEC's Oversight of Administrative Law Judges*, The CLS Blue Sky Blog (Mar. 9, 2018), https://bit.ly/2v8o6S9 (all Internet sites last visited April 11, 2018). Finality orders thus indicate not that the Commission has approved the decision, but merely that it "has not chosen to review." *E.g.*, *In re Horizon Wimba, Inc.*, Exchange Act Release No. 75,929, 2015 WL 5439958, at *1 (Sept. 16, 2015). Because 90% of ALJ decisions become final without any Commission review, *Bandimere* v. *SEC*, 844 F.3d 1168, 1180 n.25 (10th Cir. 2016), those decisions are not recommendatory—much less "purely" so, *Free Enter. Fund*, 561 U.S. at 507 n.10.

b. *Amicus* further argues (at 37) that *Freytag* is distinguishable because, he says, STJs had the contempt power. *Freytag* noted, however, only that STJs could "enforce compliance with discovery orders," 501 U.S. at 882—which SEC ALJs can do too, *see* 17 C.F.R. §§ 201.111(b), .180. *Freytag* mentioned contempt only in assessing the *Tax Court*'s status as a "court of law," *see* 501 U.S. at 891; and the statute on which *Amicus* relies provided that the Tax Court—not STJs—had contempt authority, *see* 26 U.S.C. § 7456(c). Regardless, there is no doctrinal basis for elevating contempt power to a threshold requirement for Officer status, since *most* executive Officers—including principal Officers such as SEC Commissioners—lack such power. *See ICC* v. *Brimson*, 154 U.S. 447, 488-89 (1894).

c. Other *amici* attempt to distinguish *Freytag* on the ground that STJs' findings were reviewed deferentially while SEC regulations provide that ALJs' findings may be reviewed *de novo*. *See* Constitutional and Administrative Law Scholars (CAC) Br. 25-26. But the issue of deference was "not relevant" to *Freytag*'s analysis. 501 U.S. at 874 n.3. Besides, just as the Tax Court adopted a deferential standard by procedural rule, the Commission's unwavering practice is to "accept [an SEC ALJ's] credibility finding, absent *overwhelming* evidence to the contrary," *In re Clawson*, Exchange Act Release No. 48,143, 2003 WL 21539920, at *2 (July 9, 2003) (emphasis added). Here, for example, the Commission deferred to the ALJ's credibility determinations, Pet. App. 69a-70a, even though one witness had admittedly filed a false claim against Lucia, and the other had "holes in his memory," *id.* 194a.

There is, in short, no difference of constitutional magnitude between the STJs in *Freytag* and SEC ALJs.

B. *Amicus*'s Attempt To Rewrite *Buckley* Fails

Unable to defend the judgment below under this Court's precedents, *Amicus* attempts to rewrite the *Buckley* standard by proposing that an official can be an Officer "*only* if the individual has (i) the power to bind the government or third parties (ii) in her own name." *Amicus* Br. 22 (emphasis added). While *Amicus* calls this the "historical" or "traditional" approach, it is neither. No court has ever adopted *Amicus*'s approach or anything like it—and for good reason.

Amicus's proposed test for Officer status cannot be reconciled with this Court's precedents, particularly *Freytag* and *Edmond*. And it contravenes the text and structure of the Appointments Clause, which clearly provides for a cadre of inferior Officers whose defining feature is that they are "directed and supervised" by principal Officers. *Edmond*, 520 U.S. at 663. In any event, SEC ALJs would be Officers even under *Amicus*'s proposed test.

1. *Amicus*'s Test Conflicts With Precedent

In *Freytag*, the government argued that STJs were employees who "act[ed] only as an aide to the Tax Court" because they had "no *independent* authority whatever," but instead entered only proposed findings and a proposed opinion in the type of case at bar. Resp. Br. at 29-31, *Freytag*, 501 U.S. 868 (1991) (No. 90-762). The Court unanimously rejected that argument, reasoning that the government's focus on STJs' lack of final decision-making authority:

> ignore[d] the significance of the duties and discretion that special trial judges possess. ... [S]pecial trial judges perform more than ministerial tasks. They take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders. In the course of carrying out these important functions, special trial judges exercise significant discretion.

501 U.S. at 881-82. *Amicus*'s proposed "authority to bind others in one's own name" requirement is substantively indistinguishable from the "independent authority" requirement that *Freytag* rejected.

The Court *could* have decided *Freytag* based on its alternative holding that STJs' power to enter final decisions in other cases also made them Officers. But it didn't: *Freytag*'s principal holding was that "[STJs] exercise significant" authority in administering trials. 501 U.S. at 882. The Court held only in the alternative that *even if* that authority were not significant, STJs' ability to enter final decisions in some cases also "would be" sufficient. *Ibid.*

Adopting *Amicus*'s rule, therefore, would require the Court to ignore *stare decisis* and walk away from *Freytag*'s core holding. It also would require the Court to revisit *Edmond* and *Weiss*, which held that military judges whose decisions were never final, *see Weiss*, 510 U.S. at 168, or were not final until approved by other executive Officers, *see Edmond*, 520 U.S. at 665, were Officers. Tellingly, *Amicus* never even mentions *Weiss*. And he incorrectly suggests (at 47) that *Edmond* is distinguishable because the adjudicators there purportedly could enter decisions "that became effective absent subsequent sanction by a superior officer." In fact, their decisions were always subject to

approval by the Judge Advocate General, who could "order ... review" by superior officers in every case. *Edmond*, 520 U.S. at 665 (citing 10 U.S.C. § 867(a)).

Nothing in *Buckley* or its progeny suggests a narrower definition of "significant authority." *See Buckley*, 424 U.S. at 120-36; *Freytag*, 501 U.S. at 880-82. This Court has explained that final decision-making authority is a key attribute of *principal* Officers. *See Edmond*, 520 U.S. at 665; *see also, e.g.*, *Dep't of Transp.* v. *Ass'n of Am. R.Rs.*, 135 S. Ct. 1225, 1239 (2015) (Alito, J., concurring). While discretionary authority to bind may be sufficient for Officer status, it is not necessary. *See Freytag*, 501 U.S. at 881-82. These teachings are flatly inconsistent with *Amicus*'s view (at 14-15) that inferior Officers, too, must be able to make final decisions "absent the subsequent sanction of a superior officer."

2. *Amicus*'s Test Conflicts With The Constitution

Amicus's unprecedented test also conflicts with the original meaning and structure of the Appointments Clause. Contrary to *Amicus*'s lengthy but ultimately empty exegesis, there are no "traditional" requirements that Officers be able to bind others—let alone in their own name. Indeed, the inferior Officers specified in the Appointments Clause generally lack the characteristics that *Amicus* proposes.

a. As this Court has explained, the phrase "Officers of the United States" "embrace[s] all appointed officials exercising responsibility" under federal law, *Buckley*, 424 U.S. at 131, irrespective of whether they can bind others. The original public meaning of "Officer"—derived from dictionaries, the ratification debates, and other Founding-era documents—confirms

that an "Officer" need only have "ongoing responsibility for carrying out a governmental task." Mascott Br. 3-4; *see also United States* v. *Maurice*, 26 F. Cas. 1211, 1214 (C.C.D. Va. 1823) (Marshall, C.J.) ("An office is defined to be 'a public charge or employment' and he who performs the duties of an office, is an officer").

Nineteenth-century treatises and practice did not condition Officer status on the power to bind. Rather, leading treatises selectively quoted by *Amicus* defined an "office" as a public position "invested with some portion of the sovereign functions of government, to be exercised ... for the benefit of the public." Floyd R. Mechem, *A Treatise on the Law of Public Offices and Officers* § 1, at 1-2 (1890); *see also* James L. High, *A Treatise on Extraordinary Legal Remedies* 581 (3d ed. 1896) (similar). Further, examples of officials who could not bind others but were held by this Court to be Officers are legion, including "thousands of clerks" in various departments, *United States* v. *Germaine*, 99 U.S. 508, 511 (1879), responsible for "the records, books, and papers appertaining to the office," *Hennen*, 38 U.S. (13 Pet.) at 259. *See also* Jennifer Mascott, *Who Are 'Officers of the United States'?*, 70 Stan. L. Rev. 443, 523 n.471, 528 n.508, 533 (2018).

Even *Amicus*'s own authorities (at 26-27) demonstrate that an official whose actions are subject to "subsequent sanction" by a superior can be an Officer. His primary authorities—a 2007 OLC opinion and an 1822 letter from Maine's Supreme Judicial Court—concluded that the question "is simply whether a position possesses delegated sovereign authority to act in the first instance, *whether or not that act may be subject to direction or review by superior officers*." *Officers of the United States Within the Meaning of the*

Appointments Clause, 31 Op. O.L.C. 73, 95 (2007) (emphasis added) (discussing *Opinion of the Justices*, 3 Greenl. (Me.) 481, 482 (1822)). SEC ALJs indisputably have authority to act in the first instance, subject to direction and review by the Commission. The 2007 OLC opinion fully supports the conclusion that SEC ALJs are Officers. *See* Pet. Br. 30-31; U.S. Br. 15, 17.

b. *Amicus*'s second requirement—that Officers must possess power to act in their own name—can be found in no treatise, case, or even legal opinion, let alone the text of the Appointments Clause. And early practice demonstrates that this was not a requirement of Officer status.

For example, the First Congress provided that certain department heads could "appoint" clerks "as they shall find necessary." Act of Sept. 11, 1789, § 2, 1 Stat. 68, 68. These "rank-and-file clerks" "engaged merely in tasks like recording the receipt of registration certificates from merchant ships importing goods." Mascott, *supra*, 70 Stan. L. Rev. at 462, 511. Subsequent Congresses similarly provided for the constitutional appointment of a "deputy quartermaster," Act of Mar. 3, 1795, ch. 44, § 11, 1 Stat. 430, 431 (amended 1796), and an "apothecary-general," charged with the "safe-keeping and delivery" of army medical equipment, Act of Mar. 2, 1799, ch. 27, §§ 1, 3, 1 Stat. 721, 721 (amended 1802). Petitioners are aware of no indication that these officials could bind others in any way, much less in their own name.

Amicus notes (at 33) that deputy marshals and deputy customs officials, who purportedly had "substantial authority to impact the rights of nongovernmental parties," were not appointed as Officers. But those deputies did not hold offices "established by Law," U.S. Const. art. II, § 2, cl. 2, because their duties

and salary were not "specified by statute," *Freytag*, 501 U.S. at 881, and they were not even distinct legal actors. Rather, statutes referenced the deputies only in passing, and their sole function was to assist Officers, while the Officers remained legally responsible for the deputies' actions. *See* Judiciary Act of 1789, § 27, 1 Stat. 73, 87; Act of Aug. 4, 1790, § 7, 1 Stat. 145, 155; *see also* Mascott, *supra*, 70 Stan. L. Rev. at 517-18.

c. The Framers deliberately set up a tripartite classification of officials subordinate to the President: his principal Officers, their inferior Officers, and non-Officer employees. *See* U.S. Const. art. II, § 2, cl. 2; *Buckley*, 424 U.S. at 126 & n.162. This approach recognizes the breadth and variety of functions required to run the government, and the authority to perform those functions necessarily increases as one moves up this hierarchy. *Most* federal officials "'rende[r] service to the government ... without thereby becoming its office[rs]'" because they do not wield significant federal authority. *Free Enter. Fund*, 561 U.S. at 506 n.9 (citation omitted). But those who wield *enough* power must be Officers—and that is necessarily a context-dependent question. Within the category of Officers, the Framers clearly identified a sub-category of inferior Officers who presumably outnumber their superiors. *See Edmond*, 520 U.S. at 662-63.

Amicus's proposed test would wipe out the category of inferior Officers altogether. The inability to make binding decisions marks "'inferior officers,'" "whose work" by definition "is directed and supervised" from above by a presidentially appointed, Senate-confirmed "'principal officer.'" *Edmond*, 520 U.S. at 663. Whereas principal Officers can unilaterally issue final decisions that are binding on the Executive,

the hallmark of inferior Officers is that they "have no power to render a final decision ... unless permitted to do so" by their superiors. *Id.* at 665; *accord Free Enter. Fund* v. *PCAOB*, 537 F.3d 667, 672 (D.C. Cir. 2008). In short, the only officials to pass *Amicus*'s proposed test would be *principal* Officers. Accepting that test thus would rewrite our Constitution, transforming an essential distinction between types of Officers into one between Officers and employees.

Moreover, *Amicus*'s proposed requirement that Officers have authority to bind others *in their own name* cannot be reconciled with the nature of delegated authority. Because all executive power is vested in the President, delegated authority is exercised not in the name of a subordinate Officer, but on behalf of the President (or the United States). For example, United States Attorneys—who are Officers, *Myers* v. *United States*, 272 U.S. 52, 159 (1926)—exercise executive power not in their own name, but on behalf of the United States. Appellate judges similarly speak for the court of appeals, not themselves, and issue majority opinions in the court's name. *Amicus*'s second proposed requirement, therefore, could be interpreted to read out *all* Officers from the Constitution's executive structure, since only the President actually acts in his own name.

Amicus argues (at 42-43) that because the President will be accountable for the actions of his principal Officers, there is no reason to hold the President (or, by extension, any principal Officer) accountable for the actions of inferior Officers. This confirms that *Amicus*'s proposed test reads inferior Officers out of the Constitution entirely. The Appointments Clause demands, however, that even the appointment of inferior Officers be accountable, directly or indirectly, "to

political force and the will of the people." *Freytag*, 501 U.S. at 884; *see also Edmond*, 520 U.S. at 663.

Amicus's test simply is not compatible with the Republic the Framers established. They adopted the Appointments Clause to ensure that *no one* exercising significant sovereign authority would be left unaccountable to the will of the people. Accordingly, this Court should reject *Amicus*'s unprecedented and unconstitutional test out of hand.

3. SEC ALJs Are Officers Even Under *Amicus*'s Test

Even taking *Amicus*'s test on its own terms, SEC ALJs still would be Officers because they have discretionary authority to bind in their own name.

For example, *Amicus* concedes (at 50) that SEC ALJs' authority to shape the record would suffice if it could bind the agency. That authority actually is binding because the Commission neither reviews evidence the ALJ has excluded, nor makes credibility determinations on its own. And because the SEC ALJ's decision is itself "a part of the record," 5 U.S.C. § 557(c)(3), the Commission *must* "conside[r]" the ALJ's credibility determination and cannot overturn it at will. *Univ. Camera Corp.* v. *NLRB*, 340 U.S. 474, 496 (1951).

SEC ALJs further bind private parties by issuing decisions that "become final." 17 C.F.R. § 201.360(d)(2). Because the Commission is not required to review every initial decision, its ALJs necessarily have the power to enter final decisions, at least where the Commission declines review. Although *Amicus* asserts (at 19) that SEC ALJs enter final decisions "in *the Commission's* name," they sign and en-

ter initial decisions in their own name—and the Commission publishes those decisions by authoring ALJ, *see* SEC, ALJ Initial Decisions, https://www.sec.gov/litigation/aljdec.shtml. Even when those decisions become final, they are not re-issued in the Commission's name, but are "deemed the action of the Commission," 15 U.S.C. § 78d-1(c); *see also Horizon Wimba*, 2015 WL 5439958, at *1 ("the initial decision of the administrative law judge has become the final decision of the Commission").

Other examples abound. SEC ALJs can "[i]ssue subpoenas," 17 C.F.R. §§ 200.14(a)(2), 201.111(b), which are issued in the ALJ's own name and are *themselves* binding because they create the obligation for the recipient to appear at a stated time and place. Private citizens and mere employees have no such power. SEC ALJs also can bind private parties by excluding or suspending counsel from a proceeding for "contemptuous conduct." *Id.* § 201.180(a). As *Amicus* seemingly concedes (at 49), such authority is exercised "in the ALJ's own name," and it plainly affects the rights of counsel and client alike.

Even if this Court were to adopt *Amicus*'s proposed test, therefore, SEC ALJs still would be Officers.

C. The SEC Should Be Accountable For The Appointment Of Its ALJs

Amicus's defense of the judgment below, while spirited, offers no meaningful answer to a simple question: Why *would* the Framers have exempted SEC ALJs from the Appointments Clause? Adjudicators who preside over adversarial proceedings that decide the property rights and livelihood of American citizens are precisely the sort of officials whose actions

should be "accountable to political force and the will of the people." *Freytag*, 501 U.S. at 884.

1. *Amicus* expresses concern (at 53) that SEC ALJs could lose their "independen[ce]" if recognized to be Officers. *See also*, *e.g.*, CAC Br. 30-31. That concern is misplaced.

SEC ALJs are not, and cannot be, "independent" of the President or the Commission. SEC ALJs are not Article III judges who, by constitutional design, are independent of the political branches. *See* Pet. Br. 39. Although they "exercise judgment concerning facts" and "interpret the provisions" of applicable statutes and regulations, such decisions "are typically made by officers charged with executing a statute" and, indeed, constitute "the very essence of 'execution' of the law." *Bowsher* v. *Synar*, 478 U.S. 714, 733 (1986). There would be no liability here, for example, had Judge Elliot not implemented executive policy by "creat[ing] from whole cloth" and retroactively applying a definition of "backtest," Pet. App. 111a, that the Commission agreed with by a bare 3-2 vote. Because SEC ALJs undisputedly exercise executive power, the Constitution requires that they be subject to Presidential control. *See Free Enter. Fund*, 561 U.S. at 492-95; *id.* at 517 (Breyer, J., dissenting).

Congress gave the Commission a choice: It could bring an enforcement proceeding in an Article III court, which is independent of the Commission, or before an SEC ALJ, who is not. *See* 15 U.S.C. § 78u. What the Commission cannot do is proceed before its captive adjudicators while holding them out—as it continues to do—as "independent adjudicators." SEC, Office of Administrative Law Judges, https://www.sec.gov/alj. By misleading investors, courts, and the public about the subordinate nature of its ALJs,

the Commissior seeks to evade the very "political accountability" that the Appointments Clause requires. *Edmond*, 520 U.S. at 663.

The Appointments Clause requires the President and his principal Officers (here, the SEC Commissioners) to take responsibility for the actions of their inferior Officers—to take credit for the good and suffer blame for the bad. The President (or the Commission) must also have the power to remove inferior Officers, but the question whether extant limitations on removing SEC ALJs transgress the separation of powers was not litigated below, and the Court has already "indicated that the removal issue is not properly before it." *Amicus* Br. 59. The Court should follow its established practice and consider the removal question only when and if properly presented. *Cf. Free Enter. Fund*, 561 U.S. at 507 n.10 (reserving this question).

2. *Amicus* also contends (at 39-42) that recognizing SEC ALJs to be Officers will "call into significant doubt the validity" of congressionally established commissions that supposedly exercise similar "hearing-related powers" without using Officers. Not so.

"[T]here can be no question" that non-Officers can perform investigative and information-gathering functions that "fal[l] in the same general category as those powers which Congress might delegate to one of its own committees." *Buckley*, 424 U.S. at 137. But where, as here, such functions "go beyond" this general category of powers—to include, for example, *enforcing* federal law against an individual in an adversarial trial process—an Officer is required. *Id.* at 138.

All of the commissions *Amicus* cites reflect this well-established distinction. *Compare, e.g., Proposed*

Legislation to Grant Additional Power to the President's Commission on Organized Crime, 7 Op. O.L.C. 128, 128 n.2, 138 (1983) (no Officers needed on "purely advisory" committee "survey[ing] the general nature of organized crime"), *with, e.g.*, *Constitutionality of the Ronald Reagan Centennial Commission Act of 2009*, 2009 WL 2810453, at *2 (O.L.C. Apr. 21, 2009) (Officers needed on commission performing "'clearly executive'" functions). Simply put, recognizing that non-Article III *adjudicators* are Officers, as this Court has already done in *Freytag* and *Edmond*, says nothing about the status of non-adjudicatory *investigators*.

Amicus likewise asserts (at 43) that *Buckley*'s standard is not "administrable." But *Amicus* offers no evidence of confusion in this Court, which has been unanimous virtually every time it has applied *Buckley*'s "significant authority" standard. The only "confusion" in the lower courts has arisen as a result of the divided decision in *Landry* v. *FDIC*, 204 F.3d 1125 (D.C. Cir. 2000)—which *Amicus* cannot even bring himself to cite. The Court granted certiorari in this case, however, to resolve that confusion.

Amicus's further conjecture (at 38-39) that "every government attorney, investigator, and law-enforcement officer" could become an Officer is misdirected. The possibility of closer questions as to how *Buckley* might apply to other kinds of officials is no reason to distort the law in this case involving adjudicators, where the answer is clear. As *Amicus* elsewhere concedes (at 6 n.3), the constitutional status of officials who "exercise functions different from those of SEC ALJs" simply is "not at issue here."

A straightforward application of *Freytag* in this case thus would affect only federal adjudicators who, like SEC ALJs, preside over adversarial enforcement

proceedings subject to Sections 556 and 557 of the APA. Pet. Br. 41-42. Other types of ALJs—such as Social Security Administration ALJs, who dispense federal benefits in informal, non-adversarial proceedings—perform substantially different functions and must be analyzed independently. *See, e.g.*, Ass'n of ALJs Br. 12-19; NOSSCR Br. 5, 12-13. Accordingly, the Court's decision in this case will logically extend to only about 150 ALJs, *see* Pet. Br. 41-42—or about 0.007% of the 2.1 million civilian officials in the federal government, *see* Office of Management and Budget, An American Budget: Analytical Perspectives, Budget of the U.S. Government, Fiscal Year 2019, at 65 (2018). The sky is not falling.

3. *Amicus* finally argues (at 54-58) that Congress did not intend to make SEC ALJs Officers. This Court has already said the opposite: "Congress intended to make" SEC ALJs a class of "'subordinate hearing *officers*.'" *Ramspeck* v. *Fed. Trial Exam'rs Conference*, 345 U.S. 128, 132 (1953) (emphasis added).

This Court long ago established that, where Congress says "officer," it means "constitutional officer," because if Congress meant "others than officers as defined by the Constitution, words to that effect would be used." *Germaine*, 99 U.S. at 510. *Germaine* established the baseline against which the APA and the securities laws were enacted. Because Congress referred to SEC ALJs as "officers" thirteen times, *see* Pet. Br. 35-36—not "as servant[s], agent[s], [or] person[s] in the service or employment of the government"—it intended to create a constitutional office, *Germaine*, 99 U.S. at 510.

Amicus suggests (at 54-55) that Congress used "officer" without *meaning* "Officer of the United

States." But Congress does not need to spell out "Officer of the United States within the meaning of the Appointments Clause." *See Beck* v. *Prupis*, 529 U.S. 494, 500-01 (2000) (Congress is presumed to adopt the "settled meaning" of terms). As *Amicus*'s primary authority explains, the statutory term "officer" encompasses more than constitutional Officers only where "context" indicates as much. *Steele* v. *United States*, 267 U.S. 505, 507 (1925). Context indicates the opposite here.

Congress endowed SEC ALJs with a primary function—presiding over adversarial enforcement hearings. That function otherwise can be performed only by principal Officers: the Commission as a body or individual Commissioners. *See* 15 U.S.C. §§ 77u, 78v, 80a-40, 80b-12; *see also* 5 U.S.C. § 556(b) (requiring the agency, one of its members, or an ALJ to "preside at the taking of evidence" in formal adjudication). In performing those functions, SEC ALJs are "directed and supervised" by principal Officers, *Edmond*, 520 U.S. at 663—namely, SEC Commissioners. The suggestion that SEC ALJs are on par with file clerks (or janitors) simply blinks reality.

The APA's definition of "officer" cements this interpretation by closely modeling the Appointments Clause's prescriptions for the appointment of inferior Officers. *Compare* 5 U.S.C. § 2104(a)(1), *with* U.S. Const. art. II, § 2, cl. 2. *Amicus* suggests (at 55-56) that this definition is not instructive because Congress replaced all references to hearing examiners as "officers" in the APA with "employees." But *Amicus* omits that Congress simultaneously defined "employee" to *include* all "officers." *See* 5 U.S.C. § 2105(a) (defining "employee" as "an officer and an individual

who is ... appointed in the civil service"). Those revisions thus provide no basis for treating SEC ALJs as mere employees.

By constitutional and congressional design, therefore, the Commission must accept responsibility for its ALJs.

II. THE CONSTITUTIONAL VIOLATION REQUIRES A MEANINGFUL REMEDY

No mere employee could have presided over the hearing that ruined Ray Lucia's life and career. Judge Elliot critically shaped the evidentiary record—including by crediting the testimony of two unreliable witnesses (who had never complained of being misled) and disregarding that FINRA-registered broker-dealers had repeatedly approved Lucia's presentations in advance—and held Lucia liable retroactively for violating Judge Elliot's *own* definition of "backtest" even though Lucia had explicitly disclosed the assumptions underlying his use of the term. *See* Pet. Br. 5-9. Judge Elliot even permanently exiled Lucia from his profession, despite no investor losses, misappropriated funds, or customer complaints. *See ibid.*

Because Lucia "ma[de] a timely challenge to the constitutional validity of [Judge Elliot's] appointment," he "is entitled" not only to "a decision on the merits," but *also* "whatever relief may be appropriate." *Ryder* v. *United States*, 515 U.S. 177, 182-83 (1995). The scope of such relief is undisputedly encompassed within the Question Presented. *See Amicus* Br. 58 (remedy issue is "relevant ... if the judgment below is reversed"); U.S. Mot. for Divided Arg. 4-5 (agreeing that petitioners "can address the [remedial] argument").

The Constitution itself requires a new "hearing before a properly appointed" adjudicator. *Ryder*, 515 U.S. at 188. Every *amicus* that addresses the remedial issue agrees with that core proposition. *See* J.S. Oliver Br. 20-25; WLF Br. 18-22; Cornell Clinic Br. 26. Although one *amicus* suggests a purely "prospective application of [the Court's] holding," NBLA Br. 12, that approach is unavailable here because the Court must "set aside" unlawful "agency action" on a petition for review under the APA, 5 U.S.C. § 706(2)(A); *see also Ryder*, 515 U.S. at 184-85 (rejecting "prospective application only" of Appointments Clause holding). At a bare minimum, therefore, the Court should ensure that Lucia receives an entirely new hearing before a constitutionally appointed adjudicator other than Judge Elliot. *See* Pet. Br. 42-49.

A new hearing must be truly *new*—the Commission (or an ALJ) cannot merely "ratify" the previous proceedings. The Commission has forfeited any ability to raise ratification or similar defenses in *this* case, as petitioners repeatedly have noted, with no objection by the government. *E.g.*, Pet. Br. 53; *see also id.* at 49-56 (providing additional reasons why "ratification" is unavailable).

The Commission's so-called Ratification Order nevertheless demonstrates that the Commission needs to be instructed that the Appointments Clause is a binding requirement of our founding compact, not a mere "matter of 'etiquette or protocol.'" *Edmond*, 520 U.S. at 659 (citation omitted). Despite the Commission's continuing failure to comply with the Clause, multiple ALJs have declared themselves "bound by" the Commission's erroneous pronouncement that it has "resolv[ed] any Appointments Clause claims" in pending SEC administrative proceedings.

E.g., *In re Snisky*, Admin. Proc. Rulings Release No. 5,658, at 2-3 (Mar. 26, 2018); *see also* WLF Br. 25-26 & n.10. The sting of dismissal would force the Commission to internalize that its systematic breach of the Constitution is a serious matter.

Dismissal is further warranted here because the taint of unconstitutionality reaches back to the order instituting proceedings, which required petitioners to appear "before an Administrative Law Judge." C.A.D.C. JA32. That order and all the proceedings that followed were unlawful because there were no constitutionally appointed SEC ALJs at the time. *See*, *e.g.*, J.S. Oliver Br. 27; WLF Br. 26 & n.11. Given that the process petitioners received was unconstitutional from root to blossom—and given the tremendous personal and financial cost already inflicted on petitioners—"the only reasonable remedy" is to instruct the Commission to dismiss the proceedings in their entirety. *Laccetti* v. *SEC*, — F.3d —, 2018 WL 1439616, at *4 (D.C. Cir. Mar. 23, 2018). That is particularly so because to this day no SEC ALJ has been constitutionally appointed. *See* Pet. Br. 51-53.

SEC ALJs exercise extraordinary power to affect citizens' lives through formal adjudication. They rule on evidence, apply law to facts, and issue decisions that, as here, can have devastating consequences. The Appointments Clause requires that the appointment of such officials be "accountable to political force and the will of the people." *Freytag*, 501 U.S. at 884. Because nobody was accountable for Judge Elliot when he decided Ray Lucia's fate, the Constitution demands meaningful relief.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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No. 17-130

In the Supreme Court of the United States

RAYMOND J. LUCIA, ET AL., PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

REPLY BRIEF FOR RESPONDENT SUPPORTING PETITIONERS

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REPLY BRIEF FOR RESPONDENT SUPPORTING PETITIONERS

The Commission's ALJs are "Officers of the United States" within the meaning of the Appointments Clause, U.S. Const. Art. II, § 2, Cl. 2, because they are not materially distinguishable from the special trial judges of the Tax Court, who were held to be inferior officers in *Freytag* v. *Commissioner*, 501 U.S. 868 (1991). The Commission's ALJs preside over formal hearings, create administrative records, make factual findings, draw legal conclusions, and determine liability and sanctions in the course of adjudicating disputes involving the primary conduct of private individuals. They then issue initial decisions interpreting and applying the law that, if not further reviewed, are "deemed the action of the Commission." 15 U.S.C. 78d-1(c). As in *Freytag*, these important powers constitute "significant authority pursuant to the laws of the United States." *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam).

The Court-appointed amicus curiae argues that a governmental official qualifies as a constitutional officer only if she "has been lawfully delegated authority to bind the government or third parties in her own name." Br. 23 (capitalization and emphasis omitted). In framing that test and applying it here, amicus commits two independent errors. First, although the power to bind the government or third parties on significant matters is sufficient for officer status when the official occupies a continuing position, see *Officers of the United States Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73, 77, 87 (2007) (2007 OLC Mem.), the Commission's ALJs possess that power when they issue decisions in their own name and the Commission declines to review their decisions. Second, the power to bind is not always necessary for officer status. As *Freytag* holds, it is possible for an official to be a constitutional officer because he is vested with important and distinctively sovereign functions. 501 U.S. at 881-882; see 2007 OLC Mem. 77, 90-92.

In addition to addressing whether the ALJ in this case was constitutionally appointed, the Court should address whether the statutory restraints on removing that ALJ from office unconstitutionally impair the President's ability to faithfully execute the laws. That critical question, which is fairly encompassed within the question presented, is directly implicated by the conclusion that ALJs exercise significant governmental authority. And failing to address it here could leave a cloud of uncertainty hanging over countless administrative proceedings that will be conducted by the Commission and by other agencies throughout the government. The Court should decline to address, however, the premature question of whether, upon remand to the

Commission, aspects of the prior proceedings may be ratified by a properly appointed decision-maker. Petitioners' ratification arguments are, in any event, without merit.

A. The Commission's ALJs Are "Officers Of The United States" Under The Appointments Clause

1. The Commission's ALJs can bind the government and third parties on important matters

a. Amicus is correct that a constitutional office is one in which there has been vested by law "a portion of the sovereign powers of the federal government." 2007 OLC Mem. 77; see Gov't Br. 17; Floyd R. Mechem, *A Treatise on the Law of Public Offices and Officers* § 1, at 1-2 (1890) ("A public office is the right, authority and duty, created and conferred by law, by which for a given period * * * an individual is invested with some portion of the sovereign functions of the government, to be exercised by him for the benefit of the public."). The exercise of such vested sovereign power reflects "significant authority pursuant to the laws of the United States." *Buckley*, 424 U.S. at 126. That type of authority "primarily involve[s] binding the government or third parties for the benefit of the public, such as by administering, executing, or authoritatively interpreting the laws." 2007 OLC Mem. 77. As the Court explained in *Freytag*, "[e]ven if the duties of special trial judges * * * were not [so] significant" in other respects, they would nevertheless qualify as constitutional officers because of their authority to render final decisions in certain tax proceedings. 501 U.S. at 882.

The Commission's ALJs are vested with the authority to bind the government and third parties in signifi-

cant matters for the public benefit. Whenever the Commission declines to engage in de novo review of an ALJ's initial decision, that decision "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. 78d-1(c). Thus, an ALJ's decision binds the parties unless the Commission, as a matter of discretion in most cases, chooses to modify or reverse that decision. *Ibid.*; see 17 C.F.R. 201.411(b)(2) ("The Commission may decline to review" most categories of adjudications.). Those procedures of the Commission follow the general framework set forth in the Administrative Procedure Act (APA), which provides that when an ALJ "makes an initial decision, *that decision then becomes the decision of the agency without further proceedings* unless there is an appeal to, or review on motion of, the agency within time provided by rule." 5 U.S.C. 557(b) (emphasis added).

To be sure, when no party seeks further review or the Commission denies it, the Commission has adopted a policy that it will issue an order informing the parties that the ALJ's decision has become final. But the finality regulation itself makes clear that it is the ALJ's "[initial] decision" that "becomes final upon issuance of the order." 17 C.F.R. 201.360(d)(2). And a finality order likewise states that it is the ALJ's "initial decision" that "has become final." *E.g.*, U.S. SEC, *Finality Order* 1, (July 8, 2009), https://www.sec.gov/litigation/aljdec/2009/33-9050.pdf (capitalization altered). Nor could the Commission say otherwise. By statute, if the Commission does not grant review, the ALJ's initial decision is "deemed" to be "the action of the Commission." 15 U.S.C. 78d-1(c). The regulation and finality order merely confirm what the statute already provides: absent

merits review by the Commission, it is *the ALJ's decision* that constitutes the final, binding, and judicially reviewable decision in the matter.

Amicus argues (Br. 47) that Section 78d-1(c), which is the general statute governing delegations by the Commission, does not apply to ALJs' initial decisions, but he misunderstands the statutory scheme. Subsection (a) permits delegation from the Commission to ALJs of "any of its functions" other than rulemaking, which includes the power to issue decisions; Subsection (b) reserves to the Commission the right to review those decisions; and Subsection (c) provides that ALJs' decisions are deemed to be the final action of the Commission if it declines to review them. Section 78d-1(c) thus mirrors the general APA provision through which an ALJ's "initial decision * * * becomes the decision of the agency," 5 U.S.C. 557(b), and amicus offers no reason to suppose that Section 78d-1(c) has a different scope that excludes an ALJ's initial decision. The Commission sensibly issues a finality order to notify parties that it has elected to let the ALJ's initial decision stand, but by statute it remains the ALJ's decision—now final—that binds the parties and governs their obligations.

b. Amicus further argues (Br. 22, 32-34) that officer status requires the power to bind "in her own name rather than in the name of a superior officer." That has never been a test for officer status, and adopting it would elevate form over substance. In *Freytag*, the Court paid no attention to whether the special trial judges signed their opinions in their own name or on behalf of the Tax Court. Early revenue officers who made binding decisions subject to further administrative appeal, see 2007 OLC Mem. 96, would not have been deprived of officer status if Congress had simply provided

that they acted in the name of the Treasury Secretary. Similarly here, it does not matter whether ALJs issue initial decisions in their own name (though they do, see, *e.g.*, Pet. App. 237a) or whether those decisions are later "deemed" to be action of the Commission. 15 U.S.C. 78d-1(c). If that mattered, Congress could deem *all* action by an agency's officials to be action of the Department Head, thereby withdrawing from the scope of the Appointments Clause the selection of the agency's entire workforce. Permitting important governmental functions to be vested in unaccountable officials, so long as a statute or regulation "deems" a properly appointed officer responsible, would transform the Appointments Clause from a meaningful structural safeguard into a paper tiger.

Amicus alternatively describes the test as whether officials are "act[ing] only as agents of their superiors." Br. 33. That formulation comes closer to the relevant question—*i.e.*, whether an official has his own independent authority to bind the government or third parties on significant matters. Officials who bind the government or third parties only pursuant to instructions from, or under the close supervision of, higher-ranking officials might not be constitutional officers because they lack an independent power to bind. See *Freytag*, 501 U.S. at 881-882 (noting that special trial judges exercise "significant discretion" in their tasks); see also 2007 OLC Mem. 93 ("*Buckley* did rightly indicate that discretion in administering the laws typically will constitute the exercise of delegated sovereign authority, and therefore is of course relevant.").

Here, however, the office of an ALJ is expressly created by statute, see 5 U.S.C. 3105, and is vested by statute and regulation with the authority to adjudicate disputes and then issue decisions that become final if the

Commission does not review them. See pp. 3-5, *supra*. The fact that the Commission retains the right of discretionary review does not mean that ALJs lack important authority in their own right. See *Edmond* v. *United States*, 520 U.S. 651, 663-665 (1997). Amicus is therefore wrong to suggest that an ALJ has "no power in his own office." Br. 34. Moreover, amicus correctly does not dispute that, in adjudicating disputes and issuing decisions, the Commission's ALJs exercise "significant discretion." *Freytag*, 501 U.S. at 882. ALJs thus possess both significant authority and discretion in issuing decisions that can become final and that accordingly can bind the government and third parties.

Even under amicus's agency formulation, the Commission's ALJs are constitutional officers because they are not agents of the Commission in any relevant sense. A basic premise of agency law is that "[a] principal has the right to control the conduct of the agent with respect to matters entrusted to him." Restatement (Second) of Agency § 14 (1958); see Restatement (Third) of Agency § 1.01 cmt. f(1) (2006) (Third Restatement) (power of control includes the ability "[to] state[] what the agent shall or shall not do, in specific or general terms" and "to give interim instructions or directions to the agent"). Here, the Commission does not have that kind of power to direct ALJs in the performance of their functions. The Commission may instruct an ALJ to hold a hearing or make findings on specific issues (see Pet. App. 238a-243a), or the Commission may take over a proceeding at any time and perform the functions itself. But unlike the principal in an agency relationship, the Commission cannot direct its ALJs to make particular findings or draw certain legal conclusions. Its ALJs have their own decisional authority in those matters.

Finally, amicus notes that the First Congress authorized the selection, apparently outside the constraints of the Appointments Clause, of deputy marshals, deputy collectors, and deputy surveyors, all of whom "had substantial authority to impact the rights of nongovernmental parties." Br. 32-33. Amicus is correct that those deputy positions are not necessarily appointed by Department Heads, see, *e.g.*, 28 U.S.C. 561(f) (Director of the Marshals Service may appoint "such employees as are necessary"), and this Court has stated that deputy marshals are not constitutional officers. See *Steele* v. *United States*, 267 U.S. 505, 508 (1925) ("The deputy marshal is not in the constitutional sense an officer of the United States."). But amicus does not argue that—like ALJs—those deputies had their own statutory and regulatory grants of authority; could perform their functions without direction by their superiors; or could make decisions that would become final and binding absent discretionary review by those superiors. Amicus similarly relies (Br. 33-34) on various Executive Branch opinions concluding that certain subordinate officials or contractors are not constitutional officers, or decisions of this Court holding that particular officials were not officers as a statutory matter. See *Steele*, 267 U.S. at 507 (general prohibition agent); *United States* v. *Germaine*, 99 U.S. 508, 512 (1879) (civil surgeon). But amicus does not attempt to show that those officials had authority equivalent to the Commission's ALJs.

2. The Commission's ALJs also exercise significant authority apart from their authority to bind

a. Although amicus recognizes that "sovereign authority *primarily* consists" of the power to bind the government or third parties, Br. 23 (emphasis added),

he elsewhere argues (Br. 34-43) that such authority is necessary to be a constitutional officer. "Delegated sovereign authority," however, "also includes other activities of the Executive Branch concerning the public that * * * have long been understood to be sovereign functions." 2007 OLC Mem. 77. It is possible for an official to qualify as a constitutional officer because he performs distinctively sovereign and executive functions. *Ibid.* For instance, an individual occupies a constitutional office if he possesses "the authority to represent the United States to foreign nations or to command military force on behalf of the government." *Ibid.*; see *id.* at 90-92.

Amicus notes that those particular functions "are not implicated here," Br. 23 n.8, but they confirm the general principle that the category of persons who are constitutional officers (because they are vested with sovereign authority) is broader than amicus asserts. Such authority includes offices that, even if they do not confer the ability to bind the government or third parties on important matters, "nevertheless are within the 'executive Power' that Article II of the Constitution confers, functions in which no mere private party would be authorized to engage." 2007 OLC Mem. 90-91. When Congress and the Commission conferred on the agency's ALJs the power to execute the law by adjudicating disputes with private individuals and assessing liability and sanctions, they conferred on ALJs sovereign authority no less than that possessed by the special trial judges in *Freytag*. Executive adjudication is a traditional sovereign function just as is judicial adjudication. The Commission's ALJs—like the special trial judges—perform much (or in particular cases, all) of the important work of agency adjudications.

b. Indeed, *Freytag* holds as much. Amicus argues (Br. 35-38) that the result in *Freytag* did not turn on the significance of the functions performed by special trial judges, but rather on their "authority to bind the government and private parties, in at least two respects." Br. 36. First, amicus points (*ibid.*) to the authority of special trial judges to "enter binding final judgments in their own name in some circumstances," in particular their statutory authority to "render the decisions of the Tax Court [*i.e.*, final decisions] in declaratory judgment proceedings and limited-amount tax cases." *Freytag*, 501 U.S. at 882. Second, amicus relies on the power of special trial judges "to bind the government and private parties by 'enforcing compliance with discovery orders'" through contempt sanctions. Br. 36-37 (quoting *Freytag*, 501 U.S. at 881-882) (brackets omitted). Amicus is not explicating *Freytag* but rewriting it.

i. In finding special trial judges to be constitutional officers, *Freytag* did not principally rely on their authority to enter final judgments. To the contrary, the Court *rejected* the government's argument that "special trial judges may be deemed employees * * * because they lack authority to enter a final decision." 501 U.S. at 881. That argument, the Court explained, "ignores the significance of the duties and discretion that special trial judges possess" when issuing initial decisions. *Id.* at 881-882. To be sure, the Court went on to say in *Freytag* that "[e]ven if the duties of special trial judges * * * were not as significant as we * * * have found them to be," they would qualify as constitutional officers because of their authority to render final decisions in certain proceedings. *Id.* at 882. But the Court expressly couched that as an alternative basis for its holding, after

first determining that the special trial judges were officers based on the significance of their adjudicative duties in issuing initial decisions.

ii. *Freytag*'s primary rationale did not turn on special trial judges' authority to issue contempt orders. Rather, the Court emphasized four "important functions": the judges' powers "[to] take testimony, conduct trials, rule on the admissibility of evidence, and * * * enforce compliance with discovery orders." 501 U.S. at 881-882. Here, the Commission's ALJs have the same powers. They take testimony, 5 U.S.C. 556(c)(4); 17 C.F.R. 200.14(a)(4); conduct trials, 5 U.S.C. 556(c)(5); 17 C.F.R. 200.14(a)(5), 201.111(d); rule on the admissibility of evidence, 5 U.S.C. 556(c)(3); 17 C.F.R. 200.14(a)(3), 201.111(c), 201.326; enforce compliance with discovery orders, 17 C.F.R. 201.180(a); and perform all other duties necessary to preside over complex adjudications, see *Bandimere* v. *SEC*, 844 F.3d 1168, 1178 (10th Cir. 2016) (listing ALJ duties), petition for cert. pending, No. 17-475 (filed Sept. 29, 2017).

Freytag's listing of these four important functions did not even mention the contempt power expressly. At most, that was implicit in the fourth function of "enforc[ing] compliance with discovery orders." 501 U.S. at 882. The only explicit mention of the contempt power appeared later in the Court's opinion in the discussion regarding whether the Tax Court "exercises judicial, rather than executive, legislative, or administrative, power." *Id.* at 890-891; see *id.* at 891 (noting the authority of the Tax Court "to punish contempts by fine or imprisonment" under 26 U.S.C. 7456(c)). That discussion was relevant to the Court's conclusion that the Tax Court is a "Court[ ] of Law" under the Appointments Clause, U.S. Const. Art. II, § 2, Cl. 2, such that "the Chief Judge

of the Tax Court constitutionally [may] be vested by Congress with the power to appoint" the special trial judges. *Freytag*, 501 U.S. at 884; see *id.* at 882-892.

The question of the Tax Court's status was relevant only because this Court had already concluded, earlier in its decision, that special trial judges were constitutional officers. See *Freytag*, 501 U.S. at 882 ("Having concluded that the special trial judges are 'inferior Officers,' we consider the substantive aspect of petitioners' Appointments Clause challenge."). Indeed, in discussing the contempt power, the Court spoke only of *the Tax Court's* "authority to punish contempts," *id.* at 891, not the special trial judges' authority. It would be passing strange for *Freytag* to have held special trial judges to be constitutional officers based on the contempt power (as amicus suggests), yet not to have expressly mentioned their possession of that power.

That is especially so because the "power to enforce compliance with discovery orders" extends beyond contempt. *Freytag*, 501 U.S. at 882. For example, a special trial judge also had the power to "require the production before him of evidence upon all matters embraced within his assignment," as well as to "order[] the issuance of subpoenas, as may be necessary," under Tax Court Rule 181 (1979). See *Samuels, Kramer & Co.* v. *Commissioner*, 930 F.2d 975, 986 (2d Cir.) (finding special trial judges to be officers based on their "power to enforce compliance with discovery orders," but not mentioning contempt), cert. denied, 502 U.S. 957 (1991); see also *Freytag*, 501 U.S. at 881 ("We agree with * * * the Second Circuit."). The Commission's ALJs have similar document-production and subpoena powers. See 17 C.F.R. 201.111(b) and (c). Amicus offers no reason to

believe that the Court's reference to the "power to enforce compliance with discovery orders" was limited to the contempt power.[1]

c. There is no conflict between *Freytag* and other decisions of this Court. Amicus argues (Br. 25) that under *INS* v. *Chadha*, 462 U.S. 919 (1983), a constitutional officer must take "action that ha[s] the purpose and effect of altering the legal rights, duties, and relations of persons." *Id.* at 952. But the Court used that phrase to describe *legislative* power, explaining that the power of the House of Representatives to pass a resolution overriding an Executive Branch decision was "essentially legislative in purpose and effect." *Ibid.* Amicus also relies (Br. 28-31) on other decisions of this Court in which government officials who had the power to issue binding decisions were described as, or were held to be, "officers." Those decisions had no occasion to consider, and accordingly did not address, whether the power to bind the government or private parties is *necessary* to officer status. And as amicus agrees, this Court's early Appointments Clause decisions were primarily concerned with whether Congress intended to create an "office," not whether the functions of the position were so significant that the Constitution required as much. Br. 29 (citation omitted). In sum, amicus identifies no decision of this Court—before or after *Freytag*—in which an official was vested with significant governmental authority,

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[1] Amicus correctly notes that a special trial judge's factual findings were "presumed to be correct" when reviewed by a Tax Court judge. Br. 38 n.11 (quoting T.C. R. 183(d) (2005)). But this aspect of Tax Court procedure was not a basis for the Court's Appointments Clause ruling, see *Freytag*, 501 U.S. at 874 n.3, even though it had been discussed at oral argument, Tr. at 33-41, *Freytag*, *supra* (No. 90-762).

and yet was held not to be a constitutional officer because he lacked the power to bind.

d. Amicus incorrectly argues that adhering to *Freytag* would require appointment of "every government attorney, investigator, and law-enforcement officer." Br. 38. The special trial judges in *Freytag* were constitutional officers not because their functions were significant in some colloquial sense, but because they had been authorized by statute to exercise distinctively sovereign power—namely, the power to shape formal adversarial proceedings instituted to impose civil liability on private individuals (in *Freytag*, as much as $1.5 billion, see 501 U.S. at 871 & n.1). And amicus does not argue that the Commission's ALJs can be instructed how to exercise their judgment in hearing and deciding their cases any more than could the special trial judges. As a matter of both the importance of their functions and their independent discretion in exercising them, amicus fails to show that the Commission's ALJs are analogous to all governmental officials who assist in law enforcement.

Amicus is similarly incorrect that, if the Commission's ALJs are held to be officers, it would "call into significant doubt" the practice of establishing federal investigatory and advisory commissions whose members are not appointed under the Appointments Clause. Br. 39. Some investigatory and advisory commissions may "issue subpoenas, administer oaths, collect documents, and call and examine witnesses." *Ibid.* But such commissions "cannot, in the absence of any other power, use the information to *do* anything." *Proposed Legislation to Grant Additional Power to the President's Commission on Organized Crime*, 7 Op. O.L.C. 128, 130 (1983). They cannot, for instance, "enact or execute a

law, *adjudicate a dispute*, or otherwise 'take any affirmative action which will affect an individual's rights,'" and their actions accordingly are not backed by any "coercive power." *Ibid.* (emphasis added; citation omitted); see 2007 OLC Mem. 85 & n.5, 98.

The Commission's ALJs, by contrast, use the information gathered during a hearing to adjudicate charges against a private person: They create the record, make factual findings, draw legal conclusions, and issue initial decisions on whether to impose sanctions that will be reviewed by the agency. The Commission's ALJs do not occupy a "purely advisory position," "one having no legal authority." 2007 OLC Mem. 77. To the contrary, they perform extremely important functions in service of executing the Nation's securities laws. And, conversely, if any of amicus's investigatory and advisory commissions were to depart from a purely advisory role, it would be exercising "significant authority" for purposes of the Appointments Clause, *Buckley*, 424 U.S. at 126, and its members would be constitutional officers who would require appointment in accordance with that Clause. See Office of Legal Counsel, *Constitutionality of the Ronald Reagan Centennial Commission Act of 2009*, 2009 WL 2810453, at *2 (Apr. 21, 2009); see also *id.* at *4 (proposing corrective measure to limit the Centennial Commission to "giving advice and making recommendations with respect to planning, developing and carrying out commemorative activities").

B. This Court Should Address The Constitutionality Of The Statutory Removal Restrictions For ALJs

As explained in our opening brief (at 39 & n.7), the question whether ALJs exercise significant authority, of the type that can only be exercised by constitutional

officers, naturally implicates the question whether statutory restrictions on removing them from office are permissible. Removal authority derives in part from the Appointments Clause, under "the well approved principle of constitutional and statutory construction that the power of removal of executive officers was incident to the power of appointment." *Myers* v. *United States*, 272 U.S. 52, 119 (1926). The removal issue is thus fairly encompassed within the question whether the Commission's ALJs are "Officers of the United States within the meaning of the Appointments Clause," Pet. Br. i, because answering in the affirmative entails remedial consequences in this case for both appointment *and* removal of the Commission's ALJs.

The proper remedy, should the Court agree that the Commission's ALJs are officers, would depend on whether the ALJ who presided in petitioners' case was subject to removal in conformance with constitutional constraints. Absent a ruling on the removal issue by this Court, the Court could remand to the agency for further proceedings before a properly appointed ALJ, only for petitioners to claim that the ALJ is unconstitutionally insulated from Presidential oversight. Indeed, petitioners want precisely that second bite at the apple in the event that the Commission pursues further proceedings. The public interest, however, strongly favors resolving the removal question now, to avoid the potential for a prolonged period of uncertainty surrounding the constitutionality of adversarial administrative proceedings conducted by the many agencies throughout the government in which ALJs preside.

Although neither petitioners nor amicus squarely addresses the issue, petitioners hint at their view that the Commission's ALJs are insulated from removal by

"one (or two) more" layers of legal protection "than the separation of powers will tolerate." Pet. Br. 38. Petitioners' suggestion, however, does not take account of the particular *type* of removal protection at issue. As the government previously explained (Br. 51-53), when the statutory restriction that permits removing ALJs "only for good cause established and determined by the Merit Systems Protection Board," 5 U.S.C. 7521(a), is properly construed—*i.e.*, to allow removal of an ALJ for failure to perform adequately or to follow agency policies, and to confine the Board's role to determining whether a factual basis exists for the agency's proffered grounds—Section 7521 affords a constitutionally sufficient degree of accountability and Executive Branch control in this case. This Court should adopt that construction in order to provide necessary clarity that Section 7521 leaves agency heads with constitutionally adequate authority to ensure that ALJs faithfully execute the law.

C. The Case Should Be Remanded To The Commission For Further Proceedings

Petitioners contend (Br. 49-57) that the proper disposition of this case is to direct dismissal of the proceedings against them. But the appropriate remedy for an Appointments Clause violation is a remand so that the government may proceed, if it chooses to do so, before a properly appointed officer. See, *e.g.*, *Ryder* v. *United States*, 515 U.S. 177, 188 (1995); *Intercollegiate Broad. Sys., Inc.* v. *Copyright Royalty Bd.*, 796 F.3d 111, 115-116 (D.C. Cir. 2015); cf. *Nguyen* v. *United States*, 539 U.S. 69, 83 (2003) (ordering remand due to improperly constituted court of appeals panel). Should this Court reverse the decision below on Appointments Clause grounds, it should order the court of appeals to remand

the case to the Commission, which may proceed by taking action itself or by assigning the matter to a properly appointed ALJ. See 15 U.S.C. 78d-1(a), 80b-3(e), (f), and (k). Under either option, those further proceedings would be conducted in conformance with the Appointments Clause. Although petitioners object to a potential ratification of the ALJ's actions on remand, that objection is both premature and meritless in any event.

1. On November 30, 2017, the Commission ratified the appointment of its ALJs, including the ALJ who presided in petitioners' case. See Gov't Br. 3 n.2. Petitioners ask this Court (Br. 51-53) to rule that the Commission's ratification order is invalid. That request is premature, however, because the government does not contend that the ratification order alone cured the Appointments Clause violation in this case. Neither the Commission nor the ALJ who presided despite his unconstitutional appointment has taken any action to remedy that deficiency in this particular proceeding. See Gov't Br. 3 n.2. The Court therefore should not opine on the legality of an order that has not been applied to petitioners. After the case has been remanded to the Commission, petitioners would be free to press their ratification argument in the normal course—that is, *if* the Commission chooses on remand to proceed before a ratified ALJ, and *if* that ALJ rules against petitioners. If, however, the Commission orders a new hearing before a newly appointed ALJ, or conducts the hearing itself in the first instance, petitioners' ratification challenge will be immaterial—and thus they cannot possibly be entitled to dismissal on that basis at this stage.

Petitioners are also mistaken in arguing (Br. 53) that the Commission "forfeited" its opportunity to ratify by failing to argue harmless error or ratification in the

court of appeals. Most obviously, proceedings in the court of appeals *predated* issuance of the ratification order. And even if the timing had been otherwise, arguing ratification would have been premature before the court of appeals, because the government does not contend that ratifying the ALJ's appointment alone cured the existing Appointments Clause violation in this case. The government contends only that a remand should be permitted for future proceedings before a properly appointed ALJ (or the Commission itself).

2. Petitioners' criticisms of the Commission's ratification order are, in any event, without merit. Ratification is the "adoption and affirmance by one person of an act which another, without authority, has previously assumed to do for him." 1 Floyd R. Mechem, *A Treatise on the Law of Agency* § 347, at 260 (2d ed. 1914). If an agent performs a "previous[ly] unauthorized" act on behalf of a principal, the principal or a properly authorized agent can ratify that act, at a minimum, where the principal (1) has authority to perform the act at the time of ratification and (2) had authority to perform the act at the time the agent acted. *Id.* § 354, at 263; see *FEC* v. *NRA Political Victory Fund*, 513 U.S. 88, 98 (1994); *United States* v. *Heinszen & Co.*, 206 U.S. 370, 382 (1907); see also Third Restatement § 4.04(1) & cmt. b. Under those criteria, the Commission has the power to ratify its ALJs' appointments. The previous hiring of the Commission's ALJs by the Chief ALJ was done on behalf of the Commission. See 5 U.S.C. 3105 ("Each agency shall appoint as many administrative law judges as are necessary."); APA § 11, 60 Stat. 244 (ALJs "shall be appointed by and for each agency."). And as the Head of a Department, the Commission had authority to appoint inferior officers, both at the time of the ALJ's

original selection and at the time of the Commission's ratification order. See *Free Enter. Fund* v. *Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 511 (2010).

A similar procedure was endorsed by this Court following invalidation of the appointments at issue in *Ryder*, on which petitioners rely (Br. 43-45). There, before the Court held that the civilian judges of the Coast Guard Court of Appeals were inferior officers who had not been properly appointed, the Secretary of Transportation cured the error by ratifying the judges' previous appointments and "adopting" them "as judicial appointments of [his] own." *Edmond*, 520 U.S. at 654. When this Court reviewed decisions rendered by those judges, it held that their appointments were proper. *Id.* at 666. Other courts have upheld similar ratifications following constitutional challenges, including under the Appointments Clause. See, *e.g.*, *CFPB* v. *Gordon*, 819 F.3d 1179, 1190-1192 (9th Cir. 2016), cert. denied, 137 S. Ct. 2291 (2017); *Intercollegiate Broad.*, 796 F.3d at 115-116, 118-119; *Doolin Sec. Sav. Bank, F.S.B.* v. *Office of Thrift Supervision*, 139 F.3d 203, 212-214 (D.C. Cir. 1998); *FEC* v. *Legi-Tech, Inc.*, 75 F.3d 704, 709 (D.C. Cir. 1996).

Petitioners' anti-ratification argument rests on the mistaken premise that, because the Commission's Chief ALJ was not authorized to appoint inferior officers as an original matter, the Commission may not ratify those appointments after the fact. But there would be no need to ratify the appointments if they had been proper in the first instance; the very purpose of ratification is to retroactively authorize what previously had been unauthorized. Thus, when a governmental official "could have authorized" an act in the first instance, ratification permits the subsequent adoption of the act "with the

same effect as though it had been properly done under a previous authority." *A Treatise on the Law of Public Offices and Officers* § 535, at 349-350 (quoting *State* v. *Torinus*, 49 N.W. 259, 259-260 (Minn. 1879)).

Here, there can be no doubt that the Commission could have voted to approve, or itself performed, the ALJs' original hiring and appointment at that time. See *United States* v. *Hartwell*, 73 U.S. (6 Wall.) 385, 393-394 (1868) (defendant's appointment by the assistant treasurer, "with the approbation of the Secretary of the Treasury," was consistent with the Appointments Clause). For similar reasons, a properly appointed ALJ may choose to ratify his or her own previous acts, or those of another ALJ, which had been unauthorized when taken due to the original defect in the ALJ's appointment. See *A Treatise on he Law of Agency* § 374, at 274 (one agent's unauthorized act may be ratified by an agent of the same principal who has the "general power to do himself the act which he ratifies") (citation omitted); see *CFPB*, 819 F.3d at 1185-1186, 1190-1192; *Doolin Sec. Sav. Bank*, 139 F.3d at 205-206, 212-214. If the Court chooses to address petitioners' ratification argument, therefore, the Court should reject it.[2]

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[2] Petitioners also suggest (Br. 50-51) that any further action by the Commission's ALJs would be invalid because they have not received presidential commissions and have not taken oaths of office. Petitioners offer no support for their assertion that the ALJs failed to take an oath of office, which is standard for federal officials. See 5 U.S.C. 3331. And this Court has recognized that a commission is not a constitutional prerequisite to a validly appointed officer's exercise of his powers. See *Marbury* v. *Madison*, 5 U.S. (1 Cranch) 137, 156 (1803) ("[I]f an appointment was to be evidenced by any public act, other than the commission, the performance of such public act would create the officer; and * * * [would] enable him to perform the duties without [the commission].").

* * * * *

For the foregoing reasons and those stated in our opening brief, the judgment of the court of appeals should be reversed and the case remanded for further proceedings before the Commission.

Respectfully submitted.

NOEL J. FRANCISCO
Solicitor General

APRIL 2018

No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, ET AL.,
PETITIONERS,

v.

SECURITIES & EXCHANGE COMMISSION,
RESPONDENT.

On Writ of Certiorari to the
United States Court of Appeals for the D.C. Circuit

BRIEF AMICUS CURIAE OF ADMINISTRATIVE LAW SCHOLARS IN SUPPORT OF NEITHER PARTY

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INTEREST OF AMICI CURIAE[1]

The individuals who have agreed to participate in this brief are 29 law professors who teach and write about administrative law. They have no interest in these cases or the parties except in their capacities as teachers and scholars. Their names and affiliations appear in an Addendum to this brief. They are filing this brief in support of neither party in order to call the Court's attention to pragmatic considerations of which the Court should be aware in deciding the question presented. Some of the amici believe that Administrative Law Judges (ALJs) are inferior officers, while others believe that they are properly treated as employees. All of us agree that, whatever the Court's conclusion, the result must continue to protect the independence of ALJs, consistent with the goal of the Administrative Procedure Act which created their positions.

INTRODUCTION

After presiding at a hearing, an ALJ employed by the Securities & Exchange Commission (SEC) wrote an Initial Decision in which he determined that petitioners Raymond J. Lucia et al. (Lucia) violated statutes implemented by the SEC. Lucia exercised its right pursuant to

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[1] This brief is filed pursuant to consents obtained from all parties. No person other than amici and their counsel have authored this brief in whole or in part or made a monetary contribution toward its preparation or submission.

SEC rules to obtain de novo review of that decision. 17 C.F.R. § 201.410, 201.411. The SEC conducted "an independent review of the record, except with respect to those findings not challenged on review." Pet. App. 40a. The SEC exercised the power conferred on it by the Administrative Procedure Act (APA): "On appeal from or review of the initial decision, the agency has all the powers it would have in making the initial decision." 5 U.S.C. § 557(b). In its opinion, the SEC agreed with the ALJ with respect to most but not all issues. Two Commissioners dissented with respect to one issue.

Lucia sought review of the SEC decision in the D.C. Circuit. Lucia argued, inter alia, that the SEC's decision was invalid because the ALJ who presided in the hearing was an inferior officer who was not appointed in a manner consistent with the Appointments Clause. Instead, the SEC had appointed the ALJ in a manner consistent with the APA. 5 U.S.C. § 3105 provides that "each agency" that employs ALJs "shall appoint" the ALJs who work for the agency. 5 U.S.C. § 5372 provides that the Office of Personnel Management (OPM) "shall by regulation prescribe . . . the qualifications to be required for appointment [of ALJs]." Acting under authority delegated by the SEC, the Chief ALJ at the SEC appointed the ALJ who presided in this case. That ALJ had previously been determined by OPM to be qualified to be an ALJ.

A panel of the D.C. Circuit Court of Appeals upheld the SEC decision on the basis of its conclusion that SEC ALJs are employees rather than inferior officers because their decisions at the conclusion of a hearing are only recommendations that the SEC is free to accept or reject. *Raymond J.*

Lucia Cos. v. SEC, 832 F.3d 277 (D.C. Cir. 2016), *rehearing en banc denied*, 868 F.3d 1021 (2017).

Before the Court granted the writ of certiorari in this case, the Solicitor General filed a brief in which he announced that the government had changed its position and now believes that ALJs are inferior officers who can only be appointed by Heads of Departments. The government expressed its agreement with the opinion of the Tenth Circuit in *Bandimere v. SEC*, 844 F.3d 1168, *rehearing en banc denied*, 855 F.3d 1128 (10th Cir. 2016). The Tenth Circuit held that SEC ALJs are inferior officers even though they lack the power to make final decisions because their positions, including their "duties, salary, and means of appointment," are established by statute and because they exercise significant discretion in carrying out important quasi-judicial functions.

The SEC responded to this change in the government's position the next day by issuing an order in which it ratified the appointments of ALJs that had previously been made by its Chief ALJ and ordered its ALJs to reconsider the actions they had taken in pending proceedings in their new capacity as appointees of the head of the agency. Order, In re: Pending Administrative Proceedings (Nov. 30, 2017).

SUMMARY OF ARGUMENT

The history of ALJs—and in particular, the importance of their independence within agencies, sheds important light on this case. Amici respectfully urge this Court to evaluate this case in light of the congressional purpose of ensuring the

independence and neutrality of ALJs. These features, in turn, protect the property and liberty interests at stake in agency adjudications and, ultimately, act as checks on agency power.

Congress devoted a substantial amount of time during the 1930s and 1940s to the question of how to structure agencies that engage in adjudication of regulatory disputes. That debate resulted in unanimous enactment of the Administrative Procedure Act (APA) in 1946. One of the core features of the APA was a complicated set of statutory safeguards to assure that the hearing examiners (later renamed ALJs) who were to preside over most agency hearings did not act in ways that reflected bias in favor of the agency that employed them. Congress created a multi-step process for appointing hearing examiners and imposed statutory limits on the power of agencies to manage and remove hearing examiners that were specifically designed to ensure that they had an appropriate degree of decisional independence from the agencies whose cases they were to hear.

This Court issued three opinions during the period from 1950 to 1955 in which it (1) acknowledged with obvious approval the congressional decision to create the position of hearing examiner with a degree of decisional independence from the agencies whose cases they adjudicate, (2) encouraged Congress to use independent hearing examiners to preside in all agency hearings, and (3) upheld the initial rules the Civil Service Commission (later renamed the Office of Personnel Management) issued to implement the provisions of the APA that were intended to assure that hearing examiners have an

appropriate degree of decisional independence from the agencies at which they preside.

This case was initiated in response to the SEC's use of the discretion Congress conferred on it in the Dodd-Frank Act to use its ALJs to preside in hearings in some types of enforcement proceedings. Previously, such cases were subject to adjudication exclusively in federal district courts. The shift of some enforcement cases from federal courts to the SEC gave rise to complaints that SEC ALJs were unduly biased in favor of the SEC. Ironically, to the extent that pro-agency bias is a concern, changing the status of ALJs as urged by petitioner would give the agency greater control over ALJ—precisely the outcome that Lucia purports to disavow.

The Court's holding and approach in this case have major implications for the adjudicative structure of the federal government. If the Court were to apply the Tenth Circuit test to the five SEC ALJs as the basis for a holding that they are inferior officers, federal courts would be required to apply the same test to the 1,926 ALJs who perform analogous functions at other agencies. And it would almost certainly trigger similar challenges to decisions made by the thousands of non-ALJ adjudicators (often referred to as administrative judges or AJs) who perform analogous functions at other agencies. Together, ALJs and AJs preside at hearings in millions of adjudications each year.

If, as seems likely, that iterative process yielded a series of holdings that many thousand federal employees with responsibilities that include presiding at hearings are inferior officers, federal courts would then have to decide what to do

about the cases that have been the subject of hearings presided over by those unconstitutionally appointed officers. Courts would also have to decide whether the statutory restrictions on removal of the members of this large new class of inferior officers are constitutional, an issue not before the Court in this case. The point, however, is that the stakes are sufficiently high to justify a judicial approach that preserves as much as possible the congressional design to check agency power through the use of ALJs.

ARGUMENT

I. THE METHOD OF APPOINTING ALJs AND THE STATUTORY LIMITS ON MANAGEMENT AND REMOVAL OF ALJs HAS A RICH HISTORY.

A. CONGRESS DEVOTED MUCH OF THE 1930s AND 1940s TO DESIGNING A STRUCTURE IN WHICH ALJs HAVE AN APPROPRIATE DEGREE OF DECISIONAL INDEPENDENCE.

During the 1930s and 1940s, Congress devoted a great deal of time and effort to crafting legislation to govern actions taken by federal agencies. After fifteen years of debates and studies, Congress unanimously enacted the Administrative Procedure Act of 1946 (APA). *See* George Shepherd, *Fierce Compromise: The Administrative Procedure Act Emerges from New Deal Politics*, 90 N.W. U. L. Rev. 1557 (1996).

One of the core issues that Congress resolved when it enacted the APA was the status of

the hearing examiners who were authorized to preside over oral evidentiary hearings in adjudications in the common situation in which the head of an agency did not personally preside. That issue was challenging because Congress sought to accomplish two potentially competing goals.

Members of Congress had received many complaints that the hearing examiners who presided in agency hearings prior to enactment of the APA were biased in favor of the agency and against the private parties who participated in those hearings. *See Ramspeck v. Federal Trial Examiners Conference*, 345 U.S. 128, 131-132 (1953). Congress responded to that concern by conferring on the new hearing examiners who would preside after enactment of the APA some degree of independence from the agencies for which they worked. *Id.* at 132-134.

Congress also wanted to further the potentially conflicting goal of ensuring that the agencies themselves would retain control of policy decisions in implementing their statutory directions. Congress recognized that hearing examiners who were sufficiently independent of the agency that employed them to reduce concerns of bias had the potential to usurp some of the policymaking power Congress had conferred on their agencies. Congress responded by including in the APA provisions that ensure that agencies retain the ability to make all of the policy decisions that might be raised in an adjudication in which a hearing examiner presides. *See* Paul Verkuil et al., *The Federal Administrative Judiciary*, Admin. Conf. of the United States, Recommendations and Reports, Vol. II, 770, 801-802 (1992).

During its fifteen years of deliberation about what became the APA, Congress considered many potential ways of reconciling the tension between those two potentially conflicting goals. Congress eventually settled on a combination of statutory provisions that are designed to further both goals simultaneously. The APA includes provisions that are designed to confer a degree of independence on hearing examiners by regulating the agency processes of hiring, managing, and removing hearing examiners. But it also includes a provision that ensures that agencies retain complete control of the policy implications of adjudicatory hearings by conferring on the agency the authority to substitute the agency's decision for the initial decision of the hearing examiner. Except for some changes in terminology and compensation, Congress has not made material changes in those provisions since Congress enacted them in 1946.

In the APA, Congress gave agencies the power to appoint hearing examiners, 5 U.S.C. § 3105, but it coupled that power with the power of the Civil Service Commission (the "Commission") to determine who is qualified to be a hearing examiner, 5 U.S.C. § 5372. The Commission implemented a merit-based system for determining eligibility to be a hearing examiner, and the agencies appointed hearing examiners from the list of applicants that the Commission determined to be eligible. As a result, although ALJs usually work for a single agency, they become eligible to be ALJs through a process overseen by the Commission.

In 1972, the Commission changed the name of hearing examiners to administrative law judges (ALJs). Change of Title to Administrative Law

Judge, 37 Fed. Reg. 16,787 (Aug. 19, 1972). In 1978, Congress ratified that decision by statute and renamed the Civil Service Commission the Office of Personnel Management (OPM). Pub. L. No. 95-251, 92 Stat. 183 (1978). (In the remainder of this brief we will use the terms hearing examiner and ALJ interchangeably.)

The vast majority of ALJs, 1,655 out of 1,926, work for the Social Security Administration (SSA). Because of frequent significant increases in its caseload, SSA often needs to hire large numbers of new ALJs. When SSA needs to hire more ALJs than the number of applicants that OPM has determined to be qualified to be ALJs, SSA asks OPM to reopen the process of determining who is eligible to be an ALJ. OPM responds to SSA's need by reopening the eligibility determination process. Through that process, OPM creates a new list of applicants eligible to be ALJs that is long enough to allow SSA to hire the number of new ALJs it needs to adjudicate the constantly increasing number of contested cases in which someone claims to be entitled to social security disability benefits. Agencies like the SEC routinely hire ALJs who have previously worked for SSA. Thus, the initial appointment of an ALJ is usually made by SSA from the list of eligible applicants created by OPM. Other agencies then choose ALJs from the large population of ALJs who work for SSA.

Congress also limited agency power to manage hearing examiners in several ways that are designed to confer a degree of independence on them, thereby protecting the rights of the regulated entities involved in adjudications. Congress's goal was to reduce the risk of pro-agency bias in the

process of presiding in a hearing, checking agencies' power by precluding them from using managerial tools as means of inducing hearing examiners to conduct adjudicatory hearings in ways that favor the agency and disfavor the private parties who participate in the hearings. Thus, the employing agency cannot discipline a hearing examiner, 5 U.S.C. § 7521; cannot determine the compensation of a hearing examiner, 5 U.S.C. § 5372; cannot assign a case to a hearing examiner except in rotation, 5 U.S.C. § 3105; cannot assign a hearing examiner any duties that are inconsistent with the duties and responsibilities of a hearing examiner, 5 U.S.C. § 3105; and cannot subject a hearing examiner to supervision or direction by any agency employee who engages in "the performance of investigative or prosecuting functions for an agency." 5 U.S.C. § 554(d)(2).

Finally, a disciplinary action can be taken against an ALJ "only for good cause established and determined by the Merit Systems Protection Board (MSPB) on the record after opportunity for hearing before the Board." 5 U.S.C. § 7521. Thus, although the SEC can initiate a proceeding against an ALJ, only the independent MSPB can impose any form of discipline against him or her.

At the same time that Congress protected the integrity of the hearing process by conferring a degree of independence on hearing examiners, Congress ensured that agencies retained complete control over the legal basis and policy content of any decision in an adjudication. Congress accomplished that goal by providing that a hearing examiner can make only an initial decision and that the agency has complete discretion to replace

it: "On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision." 5 U.S.C. § 557(b). This Court has reinforced that congressional decision by holding that the initial decision qualifies only as part of the record on which the court must base its review. *Universal Camera v. NLRB*, 340 U.S. 474, 493-497 (1951).

B. THIS COURT ISSUED A SERIES OF DECISIONS IN THE 1950s IN WHICH IT ENDORSED THE LEGAL REGIME GOVERNING ALJs THAT CONGRESS CREATED.

Shortly after Congress enacted the APA, this Court issued a series of decisions regarding the qualified independence of hearing examiners in which it praised the APA and urged Congress to use it as a model for all agency decision-making. In *Ramspeck v. Federal Trial Examiners Conference*, 345 U.S. 128 (1953), the Court upheld the initial rules issued by the Civil Service Commission to govern the compensation and tenure of hearing examiners, and the rules governing assignment of cases to hearing examiners, over an objection by an association of hearing examiners that the rules were not adequately protective of the independent status of hearing examiners that the APA was enacted to protect.

The six-Justice majority described the reasons Congress conferred qualified independence on hearing examiners in the APA: "Many complaints were voiced against the actions of hearing examiners, it being charged that they were

mere tools of the agency concerned and subservient to the agency heads in making their proposed findings of fact and recommendations." *Id.* at 131. The majority described studies that supported the complaints of bias and that urged Congress to make hearing examiners "partially independent of the agency by which they were employed." *Id.* at 131. The majority then described the congressional deliberations about the best ways of accomplishing that agreed-upon goal, and described with apparent approval the treatment of hearing examiners in the APA: "Several proposals were considered, and in the final bill Congress provided that hearing examiners should be given independence and tenure in the existing Civil Service system." *Id.* at 131-32.

The majority's description of the APA's treatment of hearing examiners and its characterization of the status of hearing examiners left no doubt that the majority understood and approved of the congressional decision to confer qualified independence on hearing examiners:

> Congress intended to make hearing examiners 'a special class of semi-independent subordinate hearing officers' by vesting control of their compensation, promotion and tenure in the Civil Service Commission to a much greater extent than in the case of other federal employees.

Id. at 132. The majority upheld the Civil Service rules based on its conclusion that the rules were consistent with congressional intent:

> The position of hearing examiner is not a constitutionally protected position. It is a creature of congressional enactment. The respondents have no vested right to positions as examiners. They hold their posts by such tenure as Congress sees fit to give them. Their positions may be regulated completely by Congress, or Congress may delegate the exercise of its regulatory power, under proper standards, to the Civil Service Commission, which it has done in his case.

Id. at 133.

The three dissenting Justices also implicitly approved of the congressional decision to confer qualified independence on hearing examiners. However, they would have held the rules invalid because of their belief that the rules should have gone even further in conferring qualified independence on hearing examiners:

> The Administrative Procedure Act was designed to give trial examiners in the various administrative agencies a new status of freedom from agency control. Henceforth they were to be 'very nearly the equivalent of judges even though operating within the Federal system of administrative justice.' Agencies were stripped of power to remove examiners working with them. Henceforth removal could be effected only after hearings by the Civil Service Commission. That same Commission was empowered to prescribe an examiner's

> compensation independently of recommendations or ratings by the agency in which the examiner worked. And to deprive regulatory agencies of all power to pick particular examiners for particular cases, § 11 of the Act commanded that examiners be 'assigned to cases in rotation so far as practicable * * *.' I agree with the District Court and the Court of Appeals that the regulations here sustained go a long way toward frustrating the purposes of Congress to give examiners independence.

Id. at 144 (citation omitted) (Black, J., dissenting).

The Court was even more forceful in its approval of, and praise for, the congressional decision to confer qualified independence on hearing examiners in *Wong Yang Sung v. McGrath*, 339 U.S. 33 (1950). The question before the Court was whether the APA provisions applicable to hearing examiners applied to deportation proceedings. The Court held that they did even though no statute explicitly made the APA applicable to those hearings.

The Court began by describing the widespread complaints of bias that led to the enactment of the APA and to its treatment of hearing examiners as independent of the agencies at which they preside. It also cited to the many studies that had substantiated those complaints and that had urged statutory changes to reduce the pro-agency bias. It then described the years of study and deliberation that led to enactment of the

APA by unanimous votes in both Houses of Congress. *Id.* at 37-45. The Court summarized the process through which the APA was enacted: "The Act thus represents a long period of study and strife; it settles long-continued and hard-fought contentions, and enacts a formula upon which opposing social and political forces have come to rest." *Id.* at 40.

The Court then compared the unfair and biased hearing that the government had provided in the case before the Court with the hearing before an impartial hearing examiner that the APA requires. *Id.* at 45-47. The Court even suggested that the Constitution might compel an agency to use the APA hearing procedures:

> The constitutional requirement of procedural due process of law derives from the same source as Congress' power to legislate and, where applicable, permeates every valid enactment of that body. . . .
>
> We would hardly attribute to Congress a purpose to be less scrupulous about the fairness of a hearing necessitated by the Constitution than one granted by it as a matter of expediency.
>
> Indeed, to so construe the Immigration Act might again bring it into constitutional jeopardy. When the Constitution requires a hearing, it requires a fair one, one before a tribunal which meets at least currently

prevailing standards of impartiality.

Id. at 49-50.

The Court concluded that the APA represented an effort by Congress to set forth the "currently prevailing standards of impartiality" and thereby to codify the minimum requirements of due process. *Id.* at 50. Based on that conclusion, the Court held that the provisions in the APA relating to hearing examiners applied to deportation proceedings. *Id.* at 51. In later cases, the Court relied on the reasoning in *Wong Yang Sung* as the basis to hold that the APA applies to hearings under the Interstate Commerce Act, *Riss & Co. v. U.S.*, 341 U.S. 907 (1951), and to Post Office fraud hearings, *Cates v. Haderlein*, 342 U.S. 804 (1952).

Admittedly, the Court eventually retreated from its suggestion that the APA codified due process when Congress explicitly rejected that interpretation of the Act in the process of enacting a deportation statute that authorized hearings that fell short of the procedural safeguards reflected in the APA. *Marcello v. Bonds*, 349 U.S. 302 (1955). But the Court never retreated from its belief that the APA adjudication provisions created a model of fairness by which all other agency adjudicatory procedures should be judged. Indeed, the Court upheld the procedures Congress authorized in deportation proceedings largely because it believed that Congress was "drawing liberally on the analogous provisions of the Administrative Procedure Act and adapting them to the

deportation process." *Id.* at 310.

II. ANY CHANGE IN THE STATUS OF ALJs SHOULD BE CONSISTENT WITH THE OVERRIDING GOAL OF MINIMIZING THE RISK OF PRO-AGENCY BIAS.

There are 1,931 ALJs who preside in adjudicatory hearings at present. Five are employees of the SEC. The other 1,926 preside in adjudicatory hearings conducted by 30 other agencies.[2] If this Court holds that ALJs are inferior officers, agencies and courts would then have to decide whether to acquiesce in agency-proposed methods of rehearing those millions of adjudicatory disputes, including those by the thousands of AJs whose rulings would be subject to the same challenge brought here. Even assuming some agencies could remedy the Appointments Clause deficiency in a manner similar to the SEC's approach, broader considerations related to ensuring ALJs' independence should not be overlooked.

The case before the Court is one of the many cases that were triggered by the SEC's use of the discretion Congress conferred on the agency to pursue some types of enforcement actions in adjudications before ALJs, rather than federal district judges. Professor Urska Velikonja has provided a detailed description of the manner in

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[2] *See* U.S. OPM, ALJs by Agency (Mar. 2017), https://www.opm.gov/services-for-agencies/administrative-law-judges/#url=ALJs-by-Agency.

which section 929P(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §929P(a), 124 Stat. 1376, 1862 (2010), enabled the SEC to make greater use of ALJs in some types of enforcement cases and led to the many cases in which parties who lost in those cases sought review based on alleged constitutional flaws in the appointment of the ALJs who presided in those cases. Urska Velikonja, *Are the SEC's Administrative Law Judges Biased? An Empirical Investigation*, 92 Wash. L. Rev. 315, 317-24 (2017).

In each of those cases, the SEC engaged in independent de novo review of the ALJ's decision and concluded that the defendant had violated securities laws, and it imposed sanctions on the defendant that included civil penalties. In each case, the party that was the subject of the sanctions sought judicial review of the SEC action and argued, inter alia, that the action was invalid because the ALJ was an inferior officer who had not been appointed in a manner consistent with the Appointments Clause.

In some of the cases, the party that was subject to the sanctions also argued that the SEC action was invalid because the for-cause limit on the SEC's ability to remove an ALJ violates the Vesting Clause and the Take Care Clause, as this Court interpreted those Clauses in *Free Enterprise Fund v. Public Company Accounting Oversight Board*, 561 U.S. 477 (2010). Velikonja, 92 Wash. L. Rev. at 328-30. The implicit, and in some cases explicit, allegation that ALJs are biased against the private party underlies the Appointments

Clause claims in these cases, but the private parties do not explain why they believe there is a causal relationship between the method of appointment and the presence or absence of a pro-agency bias.

The claims that SEC ALJs are biased in favor of the agency echo the widespread claims of bias that provided the impetus for Congress's decision to enact the APA. That statute reduced significantly the potential for ALJ bias in the process of presiding over agency adjudications. Ironically, the claims of bias spawned by the SEC's decision to bring some enforcement actions before ALJs, rather than federal district judges, have been coupled with the argument that SEC ALJs should be appointed by the agencies where they preside and should be removable at will by the agencies where they preside.

It is hard to imagine a worse fit between an alleged problem in decision-making and a proposed remedy for that problem. If this Court makes a decision that cascades into a legal regime in which agencies have greater discretion in the process of appointing ALJs and have the discretion to remove ALJs without establishing any cause for removal, it will have eliminated many of the safeguards against pro-agency bias that Congress incorporated in the APA and that this Court praised as important mechanisms to protect the due process rights of the private parties who participate in agency hearings. That, of course, would increase the risk that SEC ALJs will make decisions that reflect pro-agency bias in their roles

as presiding officers.

A holding that SEC ALJs are inferior officers who must be appointed by heads of departments would not necessarily conflict with the congressional goal that was the basis for the safeguards of ALJ independence that Congress incorporated in the APA as long as the initial determinations of basic qualifications continued to be made by OPM. The APA authorizes agencies to appoint ALJs, and this Court has held that the SEC qualifies as a "head of department," as that term is used in the Appointments Clause. *Free Enterprise Fund*, 561 U.S. at 512-13. Such a holding would be consistent with the critical role that Congress assigned the OPM in determining the people who have the qualifications required to be eligible for appointment by the SEC. Congress often limits the scope of the power of appointment by qualifying it in various ways, and no court has ever held that such a limit violates the Appointments Clause.[3]

But the potential removal ramifications of this series of SEC challenges cannot be ignored, because they are critical to the broader

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[3] In *FEC v. NRA Political Victory Fund*, 6 F. 3d 821, 824-25 (D.C. Cir. 1993), the D.C. Circuit held that the constitutional validity of the common statutory restriction on the President's power to appoint no more than a bare majority of the members of a multi-member agency is not justiciable. This Court dismissed the petition for writ of certiorari that was filed in the case on the basis that the FEC lacks the power to represent the United States in the Supreme Court. *FEC v. NRA Political Victory Fund*, 513 U.S. 88, 90 (1994).

considerations of neutrality underlying the ALJ provisions of the APA. Were this Court to hold ALJs to be inferior officers without using cautiously cabined analysis, a later court would likely conclude that the statutory for-cause limit on an agency's power to remove an ALJ violates separation of powers. Such a holding would have a devastating effect on the decisional independence of ALJs. As this Court has recognized, the power to remove a government official creates a "here and now subservience" between the government official and the individual or institution that has the power to remove the official. *Bowsher v. Synar*, 478 U.S. 714, 720, 730 (1986). That subservient relationship is particularly powerful when the entity that has the power to remove the official is not required to state a cause for removing the official. If the SEC could remove an ALJ without having shown good cause for removal, the risk that SEC ALJs would behave in a manner that is biased in favor of the agency would increase dramatically.

CONCLUSION

Regardless of the outcome of the Appointments Clause issue, the Court should resolve the issue in a manner that is respectful of the independent relationship between ALJs and the agencies that employ them that Congress created by passing the APA.

Respectfully submitted,

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No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA
AND RAYMOND J. LUCIA COMPANIES, INC.,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Petition For A Writ of Certiorari To The United States Court of Appeals For The District of Columbia Circuit

BRIEF OF THE AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS AS *AMICUS CURIAE* IN SUPPORT OF AFFIRMANCE OF JUDGMENT BELOW

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INTEREST OF *AMICUS CURIAE*

The American Federation of Labor and Congress of Industrial Organizations is a federation of 55 national and international labor organizations with a total membership of over 12 million working men and women.[1] This case addresses whether administrative law judges at the Securities and Exchange Commission are inferior officers within the meaning of the Appointments Clause and must, therefore, be appointed in accordance with the Clause. The unions affiliated with the AFL-CIO are significant stakeholders in the administrative decisionmaking processes of the National Labor Relations Board and of other federal agencies such as the Occupational Safety and Health Review Commission and the Federal Mine Safety and Health Review Commission, all of which rely, in part, but in diverse manners, on fact-finding by administrative law judges.

SUMMARY OF THE ARGUMENT

The question of whether administrative law judges are Officers of the United States who must be appointed in accordance with the Appointments Clause cannot be decided categorically because the answer depends on the nature of the authority exercised by particular judges. Congress, in a particular agency's enabling statute, may vest that agency's administra-

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[1] Counsel for the petitioners and counsel for the respondent have consented to the filing of *amicus* briefs. No counsel for a party authored this brief *amicus curiae* in whole or in part, and no person or entity, other than the *amicus*, made a monetary contribution to the preparation or submission of this brief.

tive law judges with specific authority. Alternatively, Congress may vest the agency's principal officers with discretion to delegate some portion of their statutory decisionmaking power to the agency's administrative law judges and the principal officers may exercise that discretion in whole or in part. In either case, this Court must examine the authority actually possessed by the specific administrative law judges at issue in order to determine if they are Officers of the United States whose appointment is governed by the Clause.

The authority administrative law judges must possess in order to be Officers of the United States is the authority to issue final decisions not subject to plenary, *sua sponte* review by superior officers. The authority to conduct fact-fidning hearings coupled with "purely recommendatory" power is not sufficient. *Free Enterprise Fund v. Public Company Accounting Oversight Board*, 561 U.S. 477, 509-10 (2010).

The National Labor Relations Act (NLRA) helpfully illustrates how the Appointments Clause applies in the context of independent agencies. Congress has twice amended the NLRA to redistribute decisionmaking power between the National Labor Relations Board (NLRB or "the Board") and lesser functionaries within the agency, specifically administrative law judges and regional directors. The result is that the Board has exercised its statutory discretion to delegate authority to conduct trials in unfair labor practice cases and to issue "a recommended order" to administrative law judges, but continues to have plenary authority under the Act to modify or set aside

any order *sua sponte*. 29 U.S.C. § 160(d); 29 C.F.R. §§ 102.35, 102.48. In contrast, the Board has exercised its statutory discretion "to delegate to its regional directors its powers" to resolve questions of representation. 29 U.S.C. § 153(b). A regional director's decision is a "final determination" not subject to plenary, *sua sponte* Board review. *Magnesium Casting Co. v. NLRB*, 401 U.S. 137, 141 (1971) (quoting 105 Cong. Rec. 19770 (statement of Senator Goldwater)). Thus, the Board's administrative law judges are non-officer employees while its regional directors are inferior officers.

As is directly relevant to this case, Congress similarly vested the Securities and Exchange Commission (SEC) with statutory authority to delegate decision making authority in certain categories of cases to its administrative law judges. Because the SEC has declined, however, to actually delegate that power—instead preserving its own authority to render final decisions in all cases—the Court below correctly determined that SEC administrative law judges, like those at the NLRB, remain non-officer employees.

Finally, even if the SEC administrative law judges were inferior officers, there would be no need for the Court to rewrite the Administrative Procedures Act to narrow its protection of administrative law judges as suggested by the Solicitor General. The agency's own discretionary choice to use administrative law judges, even if they have statutory just cause protection, does not create the type of separation of powers concerns that underlay this Court's decision in *Free Enterprise Fund*. In *Free Enterprise Fund*, Congress established the inferior offices, vested their

occupants with authority, and shielded the officers from discharge. Here, in contrast, the executive branch agency has chosen to use administrative law judges who have statutory just cause protection and chosen how much decisionmaking authority to vest in those judges. "The President can . . . choose to restrain himself in his dealings with subordinates" in this manner without implicating separation of powers concerns. 561 U.S. at 497.

ARGUMENT

I. Determining Whether Administrative Law Judges Are Officers of the United States Requires Examination of the Particular Statutory Scheme Under Which They Operate

"[T]he very size and variety of the Federal Government . . . discourage[s] general pronouncements" concerning whether particular "civil servants within independent agencies would . . . qualify as 'Officers of the United States,' who 'exercis[e] significant authority pursuant to the laws of the United States[.]'" *Free Enterprise Fund*, 561 U.S. at 506 (quoting *Buckley v. Valeo*, 424 U.S. 1, 126 (1976)). Not surprisingly, then, this Court has recognized that "[w]hether administrative law judges are necessarily 'Officers of the United States' is disputed." *Id.* at 507 n.10. As we explain below, administrative law judges within a particular agency are inferior officers only if Congress, in the enabling statute, vested the administrative law judges with final decisionmaking power or vested the agency's principal officers with authority to delegate some portion of their final decisionmak-

ing power to the agency's judges and the principal officers have done so.

A. Administrative Law Judges Are Officers of the United States Only If They Have Authority to Issue Final Decisions

Independent agencies are headed by one or more "executive 'Officers,'" *Free Enterprise Fund*, 561 U.S. at 506—principal officers who are endowed by the agency's enabling statute with some aspect of the "sovereign functions of government." *Officers of the United States Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73, 84 (2007) (quoting Floyd R. Mechem, *A Treatise on the Law of Public Offices and Officers* § 4, at 5 (1890)). This "sovereign authority" is "power lawfully conferred by the government to bind third parties, or the government itself, for the public benefit." 31 Op. O.L.C. at 87. Pursuant to the Appointments Clause, such principal officers, whose offices must "be established by law," are subject to presidential appointment "with the Advice and Consent of the Senate." U.S. Const. art. II, § 2, cl. 2.

Unlike the power to appoint principal officers—which must be exercised by the President directly—"Congress may by law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments." *Id.* In the case of independent agencies, Congress "ordinarily" vests this appointment authority in "the department head, rather than the President," *i.e.*, in the agency's principal officer. *Free Enterprise Fund*, 561 U.S. at 493. *See also Edmond v. United States*, 520 U.S. 651, 662 (1997) (noting that

"the term 'inferior officer' connotes a relationship with some higher ranking officer or officers below the President"). *Cf. id.* at 663 (citing example of "the first executive department, the Department of Foreign Affairs" in which the Secretary, the "principal officer," would be appointed by the President, and "the chief Clerk," "an inferior officer [was] to be appointed by the said principal officer").[2]

Whether a particular agency's functionaries are inferior officers who must be appointed consistent with the Appointment Clause rather than non-officer employees turns not on what actions an agency's functionaries take in any given case, but rather on the authority vested in the functionaries. *See, e.g., Freytag v. Commissioner*, 501 U.S. 868, 882 (1991) (disregarding what "duties" a functionary "on occasion performs," and looking instead to whether that functionary "is an inferior officer for purposes of [the governing statute]," in which case "he is an inferior officer within the meaning of the Appointments Clause"). In other words, the question is whether, under the agency's enabling statute, the functionaries are vested with "power . . . to bind third parties, or the government itself, for the public benefit," 31 Op. O.L.C. at 87.

As Judge Stephen Williams explained in *Landry v. FDIC*, 204 F.3d 1125, 1134 (D.C. Cir. 2000), the deci-

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[2] In the case of agencies headed by a multi-member board or commission, such as the SEC and NLRB, this Court has concluded that that body, acting as a whole, is the "Head[] of [a] Department[]" for purposes of the Appointments Clause. *Free Enterprise Fund*, 561 U.S. at 512-13.

sion on which the Court below relied, in *Freytag*, "the S[pecial] T[rial] J[udge]s' power of final decision [delegated to the STJs by the Internal Revenue Code] in certain classes of cases was critical." That is evident because "the Court laid exceptional stress on the STJs' final decisionmaking power" "even though in his case the STJ had *not* been exercising" the power, an "explanation [that] would have been quite unnecessary if the purely recommendatory powers were fatal in themselves." *Id.* (emphasis in original). Referring specifically to STJs' authority to "take testimony, conduct trials, rule on the admissibility of evidence, and . . . enforce compliance with discovery orders," this Court stated, "[t]he fact that an inferior officer on occasion performs duties that may be performed by an employee not subject to the Appointments Clause does not transform his status under the Constitution." *Freytag*, 501 U.S. at 881-82. *Accord Free Enterprise Fund*, 561 U.S. at 509-10 (stating that if the Court were to "restrict the [Public Company Accounting Oversight] Board's enforcement powers, so that it would be a purely recommendatory panel[,]" "its members would no longer be 'Officers of the United States' ").

Implicit in this reasoning is a recognition that, short of a legal delegation of the "power of final decision," it is not possible to define, and thus this Court has not specified and should not attempt to specify, the precise quantum of "purely recommendatory powers," *Landry*, 204 F.3d at 1134, necessary to distinguish between non-officer employees and inferior officers. Surely Congress does not convey "officer" status to any individual employed by the government who merely "take[s] testimony," who only "regulat[es]

document production and depositions," or who is limited to "ruling on the admissibility of evidence." *Bandimere v. U.S. Securities and Exchange Commission*, 844 F.3d 1168, 1179-80 (10th Cir. 2016). At what point, then, does the combination of these "more than ministerial tasks" add up to the "exercis[e of] significant authority pursuant to the laws of the United States"? *Freytag*, 501 U.S. at 881-82. The answer—implicit in this Court's two observations in *Free Enterprise Fund*: (1) that, "unlike members of the [Public Company Accounting Oversight] Board," who the Court assumed were Offices of the United States, "many administrative law judges . . . possess purely recommendatory powers," and (2) that "[w]hether administrative law judges are *necessarily* 'Officers of the United States' is disputed," *Free Enterprise Fund*, 561 U.S. at 507 n.10—is never.

Just as "[t]he fact that an inferior officer on occasion performs duties that may be performed by an employee not subject to the Appointments Clause does not transform his status under the Constitution[,]" *Freytag*, 501 U.S. at 882, the fact that an individual performs some more-than-ministerial, yet still recommendatory, tasks does not transform her into an Officer of the United States. As a leading early decision summarized this key distinction: "[A] delegation of a portion of the sovereign power" involves "a legal power, which may be rightfully exercised, and in its effects it will bind the rights of others, and be subject to revision and correction only according to the standing laws of the State," in contrast with a person whose acts have no "authority and power of a public act or law" absent the "subsequent sanction" of an officer or the legislature. *Opinion of the Jus-*

tices, 3 Greenl. (Me.) 481, 482 (1822). *See also* 31 Op. O.L.C. at 82-83, 95 (describing the Supreme Judicial Court of Maine's opinion as providing "the fullest early explication" of "the original meaning" of the term "public office" and noting that "[o]ther courts treated this early analysis as authoritative").

B. Examination of the NLRA and Its Legislative History Illustrates the Type of Case-by-Case Analysis Needed to Determine If Administrative Law Judges Are Officers of the United States

Congress' varying methods of distributing decisionmaking authority within different independent agencies on a statute-by-statute basis in furtherance of specific congressional policy goals is helpfully illustrated by the National Labor Relations Act (NLRA).

The principal officers of the agency created by the NLRA—all appointed by the President with the advice and consent of the Senate—are the five members of the National Labor Relations Board and the General Counsel. 29 U.S.C. §§ 153(a) & (d). The NLRA assigns two responsibilities to the Board: the prevention of unfair labor practices, 29 U.S.C. § 160, and the determination of collective bargaining representatives within appropriate bargaining units, 29 U.S.C. § 159.[3]

Under the original National Labor Relations Act of 1935 ("the Wagner Act"), Pub. L. 74-198, 49 Stat. 449,

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[3] The General Counsel is charged with investigating and prosecuting unfair labor practice complaints before the Board and supervising the agency's regional offices. 29 U.S.C. § 153(d).

451 § 3(a), Congress assigned both of these responsibilities to a three-member Board. For unfair labor practice cases, the Wagner Act permitted the Board to assign a "designated agent or agency" to conduct a hearing, testimony from which "shall be reduced to writing and filed with the Board" so that the Board could decide "[i]f upon all the testimony taken the Board shall be of the opinion that any person named in the complaint has engaged in or is engaging in any . . . unfair labor practice." 49 Stat. at 453-54, §§ 10(b) & (c). In the years that followed, the Board established the practice of using "trial examiners"[4] to conduct unfair labor practice hearings. *See, e.g., Consolidated Edison Co. v. NLRB*, 305 U.S. 197, 224-28 (1938) (describing unfair labor practice hearing before trial examiner under Wagner Act).

A little over a decade later, in response to significant congressional dissatisfaction with the NLRB decision-making process in unfair labor practice cases, Congress enacted the Labor Management Relations Act of 1947 ("the Taft-Hartley Act"), Pub. L. 80-101, 61 Stat. 136. That law substantially altered the NLRB's role vis-à-vis trial examiners, expanding the Board's responsibility to decide unfair labor practice cases itself, while cabining the role played by trial examiners.

First, the Taft-Hartley Act increased the size of the Board from three members to five and permitted the

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[4] The title "administrative law judge" was substituted for "trial examiner" in the NLRA pursuant to 5 U.S.C. § 3105 and Pub. L. 95-251, 92 Stat. 184 § 3 (March 27, 1978) (codified as a note to 5 U.S.C. § 3105). We use the two terms interchangeably in reference to the NLRB.

new five-member Board to delegate its decisionmaking power not to trial examiners, but to three-member panels of the Board itself. 61 Stat. at 139, §§ 3(a) & (b), codified as 29 U.S.C. §§ 153(a) & (b). A primary purpose of this amendment was "to increase the Board's efficiency by permitting multiple three-member groups to exercise the full powers of the Board." *New Process Steel, L.P. v. NLRB*, 560 U.S. 674, 699 (2010) (Kennedy, J., dissenting) (citing S. Rep. No. 105, 80th Cong., 1st Sess., 8 (1947)). But Congress also wanted the NLRB to take greater responsibility for its own policy decisions, perceiving the Board as "hav[ing] fallen into the habit of delegating the reviewing of transcripts of the hearings and findings of trial examiners" to others within the agency, rather than "familiariz[ing] themselves with the briefs and bills of exception" so that "the divergent views of the different [Board members] may be reflected in each decision." S. Rep. No. 105, 80th Cong., 1st Sess. 8-9, reprinted in 1 NLRB, *Legislative History of the Labor Management Relations Act, 1947* 414-15 (1948) ("Leg. Hist.").

At the same time, the Taft-Hartley Act circumscribed the role played by trial examiners, limiting them to "issu[ing] and caus[ing] to be served on the parties to the proceeding a *proposed* report, together with a *recommended* order." 61 Stat. at 147, § 10(c) (emphasis added), codified at 29 U.S.C. § 160(c). This proposed report and recommended order "shall be filed with the Board, and if no exceptions are filed within twenty days after service thereof upon such parties, or within such further period as the Board may authorize, such recommended order shall become the order of the Board and become

effective as therein prescribed." *Id.* To make clear that the decision whether to adopt a trial examiner's decision rested solely with the Board, Congress retained § 10(d) of the NLRA, stating that "the Board may at any time, upon reasonable notice and in such manner as it shall deem proper, modify or set aside, in whole or in part, any finding or order made or issued by it[,]" "[u]ntil the record in a case shall have been filed in a court." 29 U.S.C. § 160(d). On the basis of this provision, "the Board has long held that, under the plain language of Section 10(d), it has the authority to modify its orders *sua sponte*." *Dorsey Trailers, Inc.*, 322 NLRB 181, 181 (1996) (citing cases), *enf. denied on other grounds*, 134 F.3d 125 (3rd Cir. 1998).

Finally, Congress stated explicitly that "no trial examiner shall advise or consult with the Board with respect to exceptions taken to his findings, rulings, or recommendations." 61 Stat. at 140, § 4(a), codified at 29 U.S.C. § 154(a). This amendment emphasized the limited role of the trial examiner as neutral fact-finder, eliminating the then-prevailing practice of "permit[ting] a trial examiner, after his findings have alternately been assailed and defended at public hearing [before the Board], to make a final defense of his published determination behind the scenes." S. Rep. No. 105, 80th Cong., 1st Sess. 10, 1 Leg. Hist. at 416. *See also* 93 Cong. Rec. 5117, 5145, 2 Leg. Hist. at 1494 (decrying "the practice of permitting the trial examiner to argue ex parte, before the Board, in defense of his findings, after the open hearing").

A little over a decade after passage of the Taft-Hartley Act, Congress amended the NLRA again.

This time, in sharp contrast to the earlier amendments, Congress expressly "authorized [the Board] to delegate to its regional directors its powers under section 9 [29 U.S.C. § 159] to determine the unit appropriate for the purpose of collective bargaining, to investigate and provide for hearings, and determine whether a question of representation exists, and to direct an election or take a secret ballot . . . and certify the results thereof." Labor-Management Reporting and Disclosure Act of 1959, Pub. L. 86-257, 73 Stat. 519, 542 § 701(b), codified as 29 U.S.C. § 153(b). As this Court has explained—rejecting a claim by an employer that "plenary review by the Board of the regional director's unit determination is necessary at some point"—"§ 3(b) [29 U.S.C. § 153(b)] was added" for the purpose of "'expedit[ing] final disposition of cases by the Board, by turning over part of its caseload to its regional directors for final determination.'" *Magnesium Casting*, 401 U.S. at 141 (quoting 105 Cong. Rec. 19770 (statement of Senator Goldwater)).

By enabling the Board to "turn over" a portion of its statutory power to another actor within the agency "for final determination"—permitting "regional directors . . . to act in all respects as the Board itself would act" in representation cases, *id.*—Congress made clear that regional directors are inferior officers for Appointments Clause purposes. Tellingly, the NLRB treats them as such. Regional directors are appointed and subject to discharge by the NLRB General Counsel with the approval of the Board. NLRB, *Board Memorandum Describing the Authority and Assigned Responsibilities of the General Counsel of the National Labor Relations Board (Ef-*

fective April 1, 1955), 20 Fed. Reg. 2175 (April 1, 1955). Because they "exercise[] important policy-making, policy-determining, or other executive functions," 5 U.S.C. § 3132(a)(2)(E), regional directors are also members of the federal government's Senior Executive Service, meaning they are subject to being "reassigned or reviewed by agency heads." *Free Enterprise Fund*, 561 U.S. at 506-07.

The difference in statutory decisionmaking authority delegated to NLRB regional directors and to the agency's administrative law judges is laid bare by "[t]he fact that Congress in 1961 rejected a reorganization which would have delegated decision-making power in unfair labor practice cases to the hands of trial examiners subject to discretionary Board review[.]" *Magnesium Casting*, 401 U.S. at 142 (citing 107 Cong. Rec. 10223, 12905-12932). As this Court has explained, "it is unmistakably plain . . . that . . . Congress did allow the [National Labor Relations] Board to make a delegation of its authority over determination of the appropriate bargaining unit to the regional director," just as it is plain "that Congress . . . rejected a reorganization plan which would have delegated decisionmaking power in unfair labor practice cases to the hands of trial examiners." *Id.* The result is that, under the NLRA, as serially amended by Congress, NLRB regional directors are inferior officers and NLRB administrative law judges are not.[5]

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[5] Nevertheless, the NLRB itself appoints its administrative law judges consistent with the Administrative Procedures Act. *See* 29 U.S.C. § 154(a); 5 U.S.C. § 3105.

C. The SEC Administrative Law Judges Are Not Officers of the United States

Pursuant to this same statute-by-statute approach to understanding the Appointments Clause, the Court below correctly determined that SEC administrative law judges—who have a far narrower scope of authority under their governing statute than did the special trial judges at issue in *Freytag* under the Internal Revenue Code—are not inferior officers. Although the securities laws permit the SEC to delegate some decisionmaking power to its administrative law judges, the SEC has by regulation declined to do so. Because the SEC has retained final decisionmaking power for itself, its administrative law judges remain non-officer employees.

As the Court below explained, "[o]ver time Congress expanded the responsibilities of the [Securities and Exchange] Commission, and by 1960 it was administering six statutes[.]" *Raymond J. Lucia Cos. v. SEC*, 832 F.3d 277, 281 (D.C. Cir. 2016). In 1961, "the President sent Congress a proposal to allow the Commission to delegate some of its responsibilities to divisions and individuals within the Commission" and "[i]n response, Congress enacted 'An Act to Authorize the Securities and Exchange Commission to Delegate Certain Functions.'" *Id.* (citing 1961 U.S.C.C.A.N. 1351, 1351-52 (President's proposal), and Pub. L. No. 87-592, 76 Stat. 394, 394-95 (1962)).

This law provides, in relevant part, that the SEC "shall have the authority to delegate, by published order or rule, any of its functions to . . . an adminis-

trative law judge, . . . including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter." 15 U.S.C. § 78d-1(a). At the same time, the law makes clear that, "[w]ith respect to the delegation of any of its functions, . . . the Commission shall retain a discretionary right to review the action of any . . . administrative law judge . . . upon its own initiative or upon petition of a party to or intervenor in such action, within such time and in such manner as the Commission by rule shall prescribe." 15 U.S.C. § 78d-1(b). "The vote of one member of the Commission shall be sufficient to bring any action before the Commission for review." *Id.*

Declining to take full advantage of its statutory authorization to "delegate . . . any of its functions to . . . an administrative law judge, including . . . with respect to . . . determining . . . any . . . matter," 15 U.S.C. § 78d-1(a), the SEC has, by regulation, reaffirmed its authority to, "on its own initiative, order review of any initial decision, or any portion of any initial decision [issued by an administrative law judge]." 17 C.F.R. § 201.411(c). The use of the term "initial decision" to describe an administrative law judge's findings is revealing. Although, as a general matter, "[r]eview by the Commission of an initial decision shall be limited to the issues" raised by the party seeking review, agency regulations make clear that, '[o]n notice to all parties, . . . the Commission may, at any time prior to the issuance of its decision, raise and determine any other matters that it deems material." 17 C.F.R. § 201.411(d). In all cases, an administrative law judge's initial decision has no

effect until "the Commission . . . issue[s] an order that the decision has become final." 17 C.F.R. § 201.360(d)(2). *See also id.* ("The decision becomes final upon issuance of the order.").

The Court below acknowledged that, under the statute, "the Commission *could* have chosen to adopt regulations whereby an ALJ's initial decision would be deemed a final decision of the Commission upon the expiration of a review period, without any additional Commission action." *Lucia*, 832 F.3d at 286 (emphasis in original). "But that is not what the Commission has done[,]" reserving for itself both the authority "to determine whether it wishes to order review even when no petition for review is filed" and the authority to determine when "the initial decision [of the ALJ] becomes final," thus "retain[ing] full decision-making powers" for the Commission. *Id.* (citing 17 C.F.R. § 201.411(c)).

As a result, "the Commission's ALJs neither have been delegated sovereign authority to act independently of the Commission nor, by other means established by Congress, do they have the power to bind third parties, or the government itself, for the public benefit." *Id.* at 286 (citing 31 Op. O.L.C. at 87). Whatever may be true of administrative law judges in other agencies—subject to congressional direction set forth in those agencies' own enabling statutes and to delegation decisions by their own agency's principal officers—SEC administrative law judges, like NLRB administrative law judges, are employees, not inferior officers.

II. Because the SEC Has Discretion Not to Use Administrative Law Judges and to Define the Scope of Their Authority, the Judges' Statutory Just Cause Protection Creates No Separation of Powers Problem Under *Free Enterprise Fund*

Finally, it bears brief mention that the Solicitor General's suggestion that—if this Court were to find the SEC administrative law judges to be inferior officers—the Court should adopt a novel, narrowing construction of the statutory removal protections for the judges in order to avoid "serious separation-of-powers concerns," SEC Br. 39, is wholly without merit.[6] The operation of the legislative restriction on executive action in relation to the administrative law judges at issue here is easily distinguishable from the legislative intrusion on executive authority over the Public Company Accounting Oversight Board (PCAOB) at issue in *Free Enterprise Fund*, so interpretive contortion of the sort the Solicitor General suggests is not required.

The Court in *Free Enterprise Fund* made clear that the fundamental flaw with the law creating the PCAOB was that, "[w]ithout the ability to oversee the Board, or to attribute the Board's failings to those whom he *can* oversee, the President is no longer the judge of the Board's conduct." 561 U.S. at 496. Key to this conclusion, however, was that Congress man-

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[6] We agree with the Court-Appointed Amicus Curiae in Support of the Judgment Below, for the reasons stated in his brief, that the Solicitor General's argument is not properly before the Court. We present the argument above only as an additional grounds for the Court not to address the matter.

dated the creation of the Board and vested it with specified authority; the SEC had no discretion over whether to create the Board or ability to shape what it would do and, once appointed, Board members could only be removed "'for good cause shown.'" *Id.* at 486 (quoting 15 U.S.C. § 7211(e)(6)).[7] As a result, "the [SEC] Commissioners are not responsible for the Board's actions." *Id.* at 496.

In contrast, both the securities laws at issue here and the NLRA vest complete discretion in the SEC and the NLRB over whether to use administrative law judges at all. *See* 15 U.S.C. § 78d-1(a); 29 U.S.C. §§ 160(b) & (c). The NLRA, for example, permits the Board to decide that an evidentiary hearing in an unfair labor practice case should be held "before the Board or a member thereof" or "before a designated agent or agency," such as an administrative law judge. 29 U.S.C. §§ 160(b) & (c). The Board's own regulations, not the statute, vest authority in the administrative law judges and define its scope. *See* 29 C.F.R. §§ 102.35, 102.48. This form of discretionary delegation of authority by an executive agency does not create the separation of powers problem identified in *Free Enterprise Fund.*

When an executive branch agency chooses, without legislative compulsion, to employ administrative

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[7] The SEC did have statutory authority to remove functions from the PCAOB, but only as a sanction and only under limited circumstances specified in the statute. *See* 15 U.S.C. § 7217(d)(1). Indeed, this Court made clear that "the Act forbids" such removal of functions "without Commission findings equivalent to those required to fire the Board." *Free Enterprise Fund*, 561 U.S. at 505.

law judges, even when those judges are protected from removal by statute, Congress has not encroached on the executive's power. This Court explained in *Free Enterprise Fund*: "The President can always choose to restrain himself in his dealings with subordinates." 561 U.S. at 497.[8]

As a result of their discretion not to use administrative law judges at all, the SEC and the NLRB, if dissatisfied with administrative law judge decisionmaking, could simply decline to delegate cases to the judges or exercise their regulatory authority to limit the scope of administrative law judge decisionmaking. "The President could then hold the [SEC or the NLRB] to account for its supervision of the [administrative law judges], to the same extent that he may hold the [SEC or the NLRB] to account for everything else it does." *Free Enterprise Fund*, 561 U.S. at 495-96.

Even if this Court were to find the SEC administrative law judges to be inferior officers, therefore, there is no separation of powers problem under *Free Enterprise Fund* and thus no reason for this Court to rewrite the Administrative Procedures Act as the Solicitor General suggests.

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[8] Of course, such a choice is different from the president's decision to sign legislation. As this Court explained immediately after the above-quoted language, "He cannot, however, choose to bind his successors by diminishing their powers." *Free Enterprise Fund*, 561 U.S. at 497.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted,

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No. 17-130

In The
Supreme Court of the United States

RAYMOND J. LUCIA, et al.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

BRIEF OF ASSOCIATION OF ADMINISTRATIVE LAW JUDGES AS *AMICUS CURIAE* IN SUPPORT OF AFFIRMING THE JUDGMENT BELOW

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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INTEREST OF *AMICUS CURIAE*[1]

The Association of Administrative Law Judges (AALJ) represents the interests of 1460 non-supervising ALJs employed by the Social Security Administration (SSA)—nearly three-quarters of all ALJs serving across the federal government—and as such has a keen interest in this case. AALJ was founded as a professional association in 1971 and has affiliated since 1999 with the International Federation of Professional and Technical Engineers, AFL-CIO.[2]

AALJ aims to preserve the integrity and independence of the administrative judiciary. Its objectives include securing the guarantees of the U.S. Constitution, the Administrative Procedure Act, the Social Security Act, and all other federal laws; supporting the professional growth of ALJs; and improving the working conditions of ALJs through collective bargaining, political action, and other means, like participating in several notable court cases involving judicial independence.

All AALJ's activities, including the filing of this brief, further the Association's goal of protecting

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[1] This brief is filed with the written consent of all parties. No counsel for any party authored this brief in whole or in part, and no person or entity other than *amicus curiae* or its counsel made a monetary contribution intended to fund the brief's preparation or submission.

[2] Office of Personnel Management (OPM) data show 1655 ALJs serving at SSA as of March 1, 2017. *See* https://goo.gl/Vf8UV4. By March 2018, roughly 1700 ALJs (including supervisory ALJs) were serving at SSA, according to agency data.

judicial independence and preserving due process in administrative adjudication.[3]

SUMMARY OF ARGUMENT

The D.C. Circuit's judgment should be affirmed because Congress intended ALJs to be federal civil service employees, who act as impartial and independent fact-finders in building records and rendering initial decisions free from bias and political control, but lack coercive authority to bind either the government or third parties.

Because every agency's organic statute and internal deployment of ALJs are distinct, even if SEC ALJs are considered inferior officers, that ruling should not control for other ALJs; especially those like SSA ALJs who do not preside over adversarial enforcement proceedings.

The inverse proposition, however, would hold. Because SEC ALJs exercise more authority through a unique variety of agency-conferred duties than do most other ALJs, if this Court were to hold that SEC ALJs are federal employees, then the same would be true for all ALJs. Affirmance of the judgment would thus firmly shut a Pandora's Box of otherwise unending agency-by-agency litigation contesting the

[3] The Association's Constitution is available at https://goo.gl/KQNphN. AALJ's National Executive Board members are listed in the Appendix.

specific duties discharged by each agency's ALJs, and the precise nature of their appointments.

Finally, this Court should not reach the removal question, which was not pressed or passed on below and is not independently worthy of review. But if it does, it should hold that ALJ removal protections are consistent with Article II given ALJs' status as quasi-judicial officers.

ARGUMENT

I. The Decision Below Was Correct Because Congress Did Not Confer The Sovereign Power Of The United States On SEC ALJs.

The decision to create an office within the meaning of the Appointments Clause belongs in the first instance to Congress, which must "establish[] [it] by Law." U.S. Const. Art. II, § 2, cl. 2. Such establishment requires a delegation of the sovereign power of the United States to the office, meaning the authority to bind the government or the public in the name of the United States.

Congress did not confer that sort of sovereign authority on ALJs generally when it created them as a special class of employees within administrative agencies. Rather, by requiring impartial initial administrative adjudications but preserving plenary agency authority over all final decisions, Congress made plain that the sovereign authority of the United

States was vested in agency heads, not ALJs. Nor did Congress confer sovereign authority on SEC ALJs specifically, addressing them only as assistants to the Commission who lack the authority to bind the Commission or third parties.

A. Congress Creates an Office Only when It Delegates Sovereign Power in the Form of Authority to Bind the Government or Third Parties.

The line between inferior officers and employees rests on at least three constitutional minimums. The starting point is that Congress must create the office "by Law." U.S. Const. Art. II, § 2, cl. 2; *see Freytag v. Comm'r of Internal Revenue*, 501 U.S. 868, 881 (1991).

Next, under both historical and current understanding, the law must delegate some portion of the sovereign power of the United States to the officer. *See* Br. for Court-Appointed *Amicus Curiae*, at 24-25, 28 (hereafter "Court-Appointed *Amicus* Br."); *Edmond v. United States*, 520 U.S. 651, 662 (1997) ("The exercise of 'significant authority pursuant to the laws of the United States' marks . . . the line between officer and nonofficer.") (quoting *Buckley v. Valeo*, 424 U.S. 1, 126 (1976)); *Officers of the United States Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73 (2007) (hereafter "OLC Opinion"), 2007 WL 1405459, at *5-*10 (collecting sources from the Founding era and thereafter).

Finally, the authority to bind in the name of the officer (not on behalf of a superior) is an essential part of the exercise of the sovereign authority and thus of constitutional officer status. *See* Court-Appointed *Amicus* Br. 25-34; OLC Opinion, 2007 WL 140545, at *11 (surveying historical sources, case law, and other OLC Opinions to conclude that "one could define delegated sovereign authority as power lawfully conferred by the Government to bind third parties, or the Government itself, for the public benefit"); Asher C. Hinds, 1 *Hinds' Precedents of the House of Representatives* 604, 610 (1907) (describing 1899 report of the Judiciary Committee of the House of Representatives concluding that commissioners were not officers of the United States when they were "mere advisory agents" with "no power to decide any question or bind the Government or do any act affecting the rights of a single individual citizen").

B. Congress Did Not Delegate Sovereign Authority to SEC ALJs Because They Lack the Power to Render and Enforce Final, Binding Decisions.

Congress created SEC ALJs as employees, not officers, because SEC ALJs lack the authority to bind the government and third parties under either the APA or the organic statutes governing the SEC. In this analysis, the duties conferred by Congress—rather than agency rule—are the most informative, because only statutorily-conferred duties reflect Congress's intent (or not) to establish a constitutional office by

law. Considering those duties, SEC ALJs do not exercise significant authority under the laws of the United States. Their statutory duties include *neither* final decision-making authority *nor* enforcement power, unlike the special trial judges in *Freytag* (who could enforce discovery orders in all cases and make final decisions in many, 501 U.S. at 881-82).

1. The creation in the APA of ALJs (then hearing examiners) as "classified Civil Service employees," *Ramspeck v. Federal Trial Examiners Conference*, 345 U.S. 128, 133 (1953), was a grand compromise between two competing objectives: agency control and adjudicative impartiality. How Congress ultimately struck the balance confirms that ALJs are employees, not officers. ALJs assist agencies through impartial fact finding and adjudication—but the agency may disregard their determinations at will.

a. As other *amici* have well described,[4] the Administrative Procedure Act was extraordinary legislation, passed unanimously by both houses, only after "a long period of study and strife," *Wong Yang Sung v. McGrath*, 339 U.S. 33, 39-41 (1950). Among the "key objectives" of the Act was the "prevention of agency abuses of examiners' integrity and impartiality." Victor G. Rosenblum, *Contexts and*

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[4] *See, e.g.*, Br. for Administrative Law Scholars as *Amici Curiae* in Support of Neither Party, at 6-11 ("Pierce Br."); Br. for Forum of United States Administrative Law Judges as *Amicus Curiae* in Support of Neither Party, at 4-8 ("Forum Br."); Br. for Federal Administrative Law Judges Conference as *Amicus Curiae* in Support of Neither Party, at 4-7 ("FALJC Br.").

Contents of "For Good Cause" as Criterion for Removal of Administrative Law Judges: Legal & Policy Factors, 6 W.N. ENG. L. REV. 593, 609 (1984). Congress thus placed "trial examiners, and other similar employees" in the civil service to prevent political appointments to these positions. *Administrative Procedure: Hearings Before a Subcomm. of the S. Comm. On the Judiciary*, 77th Cong. 250, 876, 1000 (1941).

Although protected from political interference, Congress intended the ALJ to still serve as a "member of a regulatory team—independent of the agency to be sure . . . but nonetheless subordinate in the sense that his work must mesh with and adapt to conform itself to the role and responsibility of the agency." Rosenblum, *supra*, at 616-17 (quoting Horsky & Mahin, *The Operation of the SSA Administration and Decisional Machinery* (1960) (mimeo)).

This balance between adjudicative independence and regulatory control is reflected in the duties assigned to ALJs by the APA. ALJs preside over fact-finding hearings at which evidence will be taken, 5 U.S.C. § 556(c) (list of presiding-employee tasks), have a duty to act impartially, *id.* § 556(b) ("The functions of presiding . . . shall be conducted in an impartial manner."), and issue initial decisions (if tasked by their agency to do so), *id.* § 557(b).

But ALJs cannot bind the agency, which has plenary authority regardless of any ALJ act or decision. 5 U.S.C. § 557(b) ("On appeal from or review of the initial decision, the agency has all the powers which it

would have in making the initial decision . . . "); *see also* U.S. Dep't of Justice, *Attorney General's Manual on the Administrative Procedure Act* 83 (1947) (the agency retains "complete freedom of decision—as though it had heard the evidence itself"); KENNETH CULP DAVIS, 2 ADMIN. L. TREATISE §§ 10.02-03 (1958) (noting the "APA clearly maintains the examiner in a subordinate position" in part because the "initial decision can rise no higher than a recommendation").

Consistent with their role as impartial hearing officers, ALJs also cannot bind private parties. No ALJ decision becomes the final decision of the agency without the agency's consent. 5 U.S.C. § 557(b).[5] And ALJs lack enforcement power (for interim or final decisions) in the form of contempt or otherwise. If a party ignores an ALJ-issued subpoena, the ALJ has no mechanism to compel it to submit. Rather, the agency itself (not the ALJ) ordinarily must go to court to obtain that compulsion. *See, e.g.*, 15 U.S.C. § 78u(e) (application to court by SEC to enforce orders). The

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[5] It is irrelevant whether agency consent is exercised through an affirmative post-decision act, a blanket policy accepting all decisions in certain categories, or silent acquiescence. Regardless of procedure, the agency—not the ALJ—holds the sovereign power. If the only criterion for officer status were the ability to make a "final" decision that stands as the agency's absent a further affirmative act, it would prove far too much, because many decisions are made every day by undisputed agency employees (like the initial examiners for disability claims, *see* p. 20, *infra*), that are never appealed and never even reach the ALJ level. Simply because some agency decisions become final without express action by the agency head does not transform employees making those decisions into constitutional officers.

same is true for an ALJ decision that the agency has opted to allow to become final without review; it is not enforceable without independent agency action (and, often, an order from an Article III court). *See id.*; pp. 16-17, *infra* (discussing enforcement of orders for other agencies).

The absence of the authority to bind confirms that Congress did not delegate sovereign power of the United States to ALJs. ALJs are instead unique civil service employees insulated from political influence through tenure and removal protections. They are insulated "from political interference," *Butz v. Economou*, 438 U.S. 478, 513 (1978), and are "not to be paid, promoted, or discharged at the whim or caprice of the agency or for political reasons." *Ramspeck*, 345 U.S. at 142. But they are not shielded from plenary agency policy control, and serve as front-line, advisory adjudicators—not final decision-makers.

Such plenary control over regulatory policy and administrative outcomes maintains complete political accountability within the Executive Branch for the exercise of executive power by the agency, fulfilling the objective of the Appointments Clause. *See Edmond*, 520 U.S. at 663 (the Appointments Clause is "designed to preserve political accountability relative to important Government assignments"). The mere assistance of employees, private industry, or other advisors in carrying out agency functions does not transform those assistants into officers. Providing support to the exercise of power is not the exercise of power. This Court in *Sunshine Anthracite Coal Co. v. Adkins*, 310

U.S. 381, 399 (1940), thus held that the Appointments Clause is not implicated when individuals "function subordinately to the [agency]" and were not entrusted with "law-making" power.

b. The fact that ALJ duties are fungible (and, by congressional design, variable) across agencies, reinforces that Congress did not contemplate a specific office wielding sovereign authority when it created the ALJ corps. Rather, Congress created a special class of federal employees to be impartial (but not final) fact-finders, with an elevated, universal skill set, and specific duties assigned by the agency.

Uniform qualification and examination criteria, 5 U.S.C. § 1104(a)(2), and the possibility of ALJ transfer between agencies, 5 C.F.R. § 930.204(h), *see also* 5 U.S.C. § 3344 (permitting temporary detail of ALJs from one agency to another)—most often from SSA, the largest employer of ALJs, to other agencies, *see* Pierce Br. 9—confirm the employee status of ALJs. ALJs are selected through a centralized process, where OPM, a neutral civil service agency, administers an examination for those eligible for a generic position based on objective qualification criteria. Agencies then select from an OPM certification that contains at least the three highest ranking candidates for the geographical location where they are hiring. *See* 5 U.S.C. § 1104(a)(2); FALJC Br. 7-9 & App. C (describing selection process). OPM's centralized certification process is further proof that Congress did not consider ALJs to be inferior officers, because the principal officers whom they serve do not fully control their

selection. Congress set no prescribed hierarchy as would typify a principal/inferior officer relationship.

2. Consideration of the authority conferred on SEC ALJs under the Commission's organic statutes does not alter the outcome. Although some of the authorities exercised by SEC ALJs are unique among ALJs, *see* part II.B, *infra*, the statutes governing SEC ALJs in the main strike the same balance as within the APA: the SEC may work through ALJs (or other employees) to accomplish its functions, 15 U.S.C. § 78d-1(a), but the Commission itself always retains the final decision authority. *Id.* § 78d-1(b). That leaves SEC ALJs without the authority to bind, making them fall on the employee side of the employee-officer line. *See* Court-Appointed *Amicus* Br. 44-51.

Neither the APA, 5 U.S.C. § 556(c), nor the statutes specific to the SEC, confer "significant authority pursuant to the laws of the United States," *Edmond*, 520 U.S. at 662 (internal citation omitted), on SEC ALJs. And the duties highlighted by Petitioner (Br. 21-23) that suggest greater authority for SEC ALJs are created by agency rule, not by statute. They do not reflect a congressional decision to delegate sovereign power to SEC ALJs. What's more, even those rule-based duties have been cut back in recent years, as Petitioner acknowledges. For example, the power to issue default orders (including default orders that levy sanctions and cease-and-desist obligations) is conferred by rule, but (as noted by Petitioner (Br. 32)), the Commission has, since 2013, mandated that ALJs can issue only initial decisions in such circumstances,

which require Commission action to take effect. *See* Exchange Act Release No. 70,708 (Oct. 17, 2013). Accordingly, SEC ALJs do not possess authority to issue binding default orders.

The power of redressing contemptuous conduct, 17 C.F.R. § 201.180(a), is likewise conveyed by rule, not by statute, and is very limited (and subject to *de novo* review). *See* Court-Appointed *Amicus* Br. 9. Moreover, this outlier rule should not control the constitutional analysis under the Appointments Clause, where Congress itself has declined to confer any enforcement authority on ALJs, *see* 5 U.S.C. § 556(c). Although Congress contemplated that agencies could assign additional duties related to presiding over hearings to ALJs, 5 U.S.C. § 556(c)(11), that narrow provision does not grant the agency license to establish an "office" in the absence of more explicit congressional authorization. To the extent that some SEC rules may stretch too far, the result should be that the rules are invalid, rather than undercutting Congress's careful assignment of limited powers to ALJs.

II. Any Ruling That SEC ALJs Are Inferior Officers Should Not Control For ALJs In Other Agencies.

For the reasons described above, all ALJs are employees. But if the Court concludes otherwise for SEC ALJs given their agency-conferred duties and responsibilities, that function-specific analysis should not control for ALJs from other agencies, because every

agency deploys its ALJs differently. There can be no one-size-fits-all functional approach to the Article II question. *Cf. Free Enterprise Fund v. Public Co. Acctg. Oversight Bd.*, 561 U.S. 477, 506-07 (2010) ("[T]he very size and variety of the Federal Government . . . discourage general pronouncements" on separation-of-powers questions not specifically presented).

A. The "Significant Authority" Test May Play Out Differently across Agencies when Agency-Specific ALJ Duties Are Considered.

Petitioner argues that only ALJs tasked by their agency to preside over adversarial enforcement proceedings are inferior officers, taking pains to exclude other ALJs from the reach of his argument. *E.g.*, Pet. Br. 41-42. Rightly so. ALJ authority, particularly the authority to bind others, is arguably greater when presiding over adversarial enforcement proceedings. But even for such proceedings, each agency differs in how much authority ALJs are permitted to wield.

This Court's cases, as well as the parties' careful parsing of the specific duties and functions of SEC ALJs here, confirm that the Appointments Clause analysis is fact-specific and contextualized. Yet the Government's brief, as well as some *amici*, suggest that the constitutional analysis would be the same for

all ALJs across every agency. AALJ respectfully disagrees.

As Justice Frankfurter observed, the APA established a "mood" that "must be respected . . . [that] can only serve as a standard for judgment and not as a body of rigid rules assuming sameness of applications." *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 487 (1951). Thus, although every ALJ is subject to the same selection criteria, *see* 5 U.S.C. § 1302; 5 C.F.R. Part 930, once placed within a given agency, the duties ALJs perform vary tremendously. Some, like those at the SEC, preside over adversarial enforcement proceedings, while others, like the majority of ALJs who work for the Social Security Administration, determine eligibility for government benefits. Still others hear regulatory matters, *e.g.*, FCC hearings on licenses under 47 U.S.C. §§ 312, 309(k); or FERC hearings resolving rate disputes, 18 C.F.R. §§ 385.206-.207.[6]

ALJ duties can also vary *within* agencies. When upholding intra-agency grade differences for ALJs, the Court in *Ramspeck* noted the different roles

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[6] *See generally* Daniel Solomon, *Summary of Administrative Law Judge Responsibilities*, 31 J. NAT'L ASSOC. OF ADMIN. LAW JUDICIARY 475 (2011); *see also* Kenneth Barnett, *Against Administrative Judges*, 49 U.C. DAVIS L. REV. 1643, 1652 & n.42 (2016). Beyond ALJs, whose independence is preserved by the APA, agencies also employ a far greater number of Administrative Judges (AJs), who often perform the same functions, and who are typically agency attorneys. *See generally id.* Whether or not sound policy, agencies' use of employee AJs interchangeably with APA ALJs is another indication of ALJs' employee status.

Civil Aeronautics Board ALJs played in safety versus economic cases, as well as differences between the "relatively simple applications for extensions" of certificates heard by ICC ALJs and other ICC proceedings "involv[ing] complicated and difficult railroad rate" determinations. 345 U.S. at 134. A functional approach to the Appointments Clause analysis, thus, might yield different results for ALJs even within the same agency.

There are also differences in how each agency appoints its ALJs; none addressed in this record. So even if this Court concludes that SEC ALJs are inferior officers and that their appointment was unconstitutional, such a holding cannot govern other ALJs for the additional reason that it is unclear how other agencies appoint their ALJs.

Here, it took years of litigation culminating in an affidavit ordered from the Commission's Deputy Chief Operating Officer to divulge the SEC's own ALJ appointment procedures. Pet. App. 298a-299a. The process would likely be no less complicated for the 30 other agencies that employ ALJs. Each, including SSA, has its own internal appointment process that is not necessarily prescribed by statute or even published rule, and that can and does change over time.

The absence of any statutory mandate governing individual agency internal hiring procedures, once ALJs have been selected by OPM, is yet further proof that Congress, in enacting the APA, did not consider

ALJs constitutional officers that required appointment in conformance with Article II.

B. SEC ALJs Exercise Significantly More Authority than Most Other ALJs.

Because SEC ALJs exercise a greater array of functions and are vested with more discretion by agency rule than other ALJs, including other ALJs who preside over adversarial enforcement proceedings, Petitioner's attempt to paint all adversarial-hearing ALJs with the same brush fails.

SEC judges are among the few ALJs (about 150) who preside over adversarial enforcement proceedings. And the expansive jurisdiction of SEC ALJs, their ability to order significant monetary penalties, and the fewer procedural protections afforded to respondents in SEC adjudications all provide greater authority to SEC judges and distinguish them from their ALJ counterparts in other agencies.

As others have chronicled,[7] SEC ALJs have authority to impose substantial monetary penalties through administrative proceedings, including the power to order disgorgement, 15 U.S.C. § 77t. SEC ALJs also have cease-and-desist powers—that is, powers prohibiting licensed firms and persons from

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[7] *E.g.*, Br. of Urska Velikonja & Joseph A. Grundfest as *Amici Curiae* in Support of Neither Party, at 7-8 (describing the Commission's expanding authority to seek monetary penalties since 1990, culminating in civil fines against non-registered entities under the Dodd-Frank Act).

violating the securities laws—and the ability to revoke licenses or bar defendants from doing securities-industry work. 15 U.S.C. § 77h-1. Although this power is always subject to the plenary authority of the SEC, it still outstrips the authority of ALJs in other agencies, largely because those other agencies are themselves less powerful than the SEC.

For example, the Federal Trade Commission and the International Trade Commission use ALJs for administrative enforcement proceedings but must seek civil penalties in a federal district court. 15 U.S.C. §§ 45(l), (m) (FTC); 19 U.S.C. § 1337(f) (ITC). The National Labor Relations Board, too, can enforce its orders remedying unfair labor practices only on application to a court of appeals. 29 U.S.C. §160(e).

Unlike many other agencies, SEC ALJs also have jurisdiction over non-regulated entities, 15 U.S.C. §§ 78o, 78o-4, 78q-1, 80b-3, and may impose (with SEC consent) monetary penalties on any individual who "is violating, has violated, or is about to violate any provision of this [title] [*id.* §§ 77a *et seq.*], or any rule or regulation thereunder." *Id.* § 77h-1(a). By comparison, other agencies are far more limited in their jurisdiction. *E.g.*, 24 C.F.R. § 100.10 (HUD's jurisdiction in Fair Housing Act cases limited to licensed or regulated businesses).

SEC ALJs also have some unique authorities under agency procedural rules. For example, SEC internal rules empower its ALJs to limit dispositive motions in 120-day proceedings, where motions for

summary disposition are available "only with leave of the hearing officer." 17 C.F.R. § 201.250(c). By contrast, dispositive motions are available without ALJ leave in other agency adjudications. *E.g.*, Consumer Financial Protection Bureau (CFPB), 12 C.F.R. § 1081.212(c); Federal Trade Commission, 16 C.F.R. § 3.24(a); Office of Financial Institution Adjudication/Federal Reserve, 12 C.F.R. § 263.29(b); and Commodity Futures Trading Commission, 17 C.F.R. § 10.91(a).

There are also fewer immediate checks on an SEC ALJ's power when compared to otherwise analogous counterparts (like the CFPB). Specifically, if a party moves to disqualify an SEC ALJ, the ALJ will rule on the motion and may continue the proceeding if the motion is denied. 17 C.F.R. § 201.112(b). Interlocutory appeals are "disfavored," and the Commission grants such appeals "only in extraordinary circumstances." *Id.* § 201.400(a). But if a party moves to disqualify a CFPB ALJ, the ALJ must certify the motion to the CFPB Director for a "prompt determination" on disqualification if he or she does not self-disqualify. 12 C.F.R. § 1081.105(c).

Finally, SEC ALJs can find that a party has defaulted for a wide range of conduct and can enter a default (subject to SEC confirmation) if a party fails to cure a deficient filing within a specified time. 17 C.F.R. § 201.155(a)(3). But a CFPB ALJ can find a party in default only where the party does not file an answer, 12 C.F.R. § 1081.201(d), or fails to appear, *id.* § 1081.203(e).

These differences in ALJ authority in adversarial enforcement actions pale in comparison to the differences across agencies in usage of ALJs more generally. As Petitioner recognizes, ALJs who run adversarial enforcement proceedings cannot be lumped together with ALJs who conduct other types of proceedings for purposes of the Article II analysis. Examining in more detail the work done by SSA ALJs, who far outnumber all other ALJs, helps explain why.

C. SSA Judges Exemplify Why ALJs Are Not Inferior Officers.

1. SSA ALJs are arguably the quintessential ALJs. SSA adjudicators served as the model for APA hearing examiners. *See Richardson v. Perales*, 402 U.S. 389, 409 (1971). And most ALJs start at the Social Security Administration before moving to positions at other agencies. The roughly 1700 ALJs working for SSA far outnumber their peers in other agencies and preside over non-adversarial administrative adjudications brought under the Social Security Act. *See* 42 U.S.C. § 405(b)(1).[8]

As then-Commissioner Astrue testified in 2012, a "key component of the integrity of [the SSA] hearings process is that ALJs act as independent adjudicators—who fairly apply the standards in the Act and our regulations. We respect the qualified decisional

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[8] *E.g.*, Titles II, VIII, XVI, XVIII of the Social Security Act, 42 U.S.C. §§ 401 *et seq.*, *id.* §§ 1001 *et seq.*, *id.* §§ 1381 *et seq.*, *id.* §§ 1395 *et seq.*

independence that is integral to the ALJ's role as an independent adjudicator." Statement of Michael J. Astrue, Commissioner, SSA, before the Committee on Ways and Means Subcommittee on Social Security, June 27, 2012 (Astrue Testimony).[9]

a. SSA ALJs are involved in one phase of an administrative process that has been described as "unusually protective" of disability claimants. *Heckler v. Day*, 467 U.S. 104, 106 (1984). An on-the-record hearing before an SSA ALJ is the *third* stage of agency review, occurring only after a claimant has been twice-denied benefits at the State level. *See generally* Astrue Testimony, *supra* (explaining the four-stage administrative review process); *see also Richardson*, 402 U.S. at 392-98 (detailing one claimant's path through the multi-level administrative process).

The hearings are non-adversarial. This Court has previously observed that "the differences between courts and agencies are nowhere more pronounced than in Social Security proceedings." *Sims v. Apfel*, 530 U.S. 103, 110 (2000) (plurality op.). Unlike Article III judges, or other ALJs who preside over adversarial enforcement proceedings, SSA ALJs are oft-said to wear three hats, because in presiding over SSA non-adversarial hearings, they act as "(1) a judge, (2) a representative of the government who cross examines the claimant, and, (3) an adviser to the claimant, required by regulation to fully develop the case to see that the claimant has a fair hearing regardless of whether the

[9] *Available at* https://goo.gl/Wrgs24.

claimant is represented by counsel or otherwise." *Salling v. Bowen*, 641 F. Supp. 1046, 1053 (W.D. Va. 1986); *see also Sims*, 530 U.S. at 110-11 (describing Social Security proceedings as inquisitorial rather than adversarial, and the ALJ's duty as investigative).

This independent "duty to inquire," *Heckler v. Campbell*, 461 U.S. 458, 471 (1983) (Brennan, J., concurring), exemplifies the core fact-finding and record-building functions of ALJs as originally contemplated under the APA, and further indicates the ALJ's employee status. *See* 1 *Hinds' Precedents* at 607-08 (1899 report concluding that certain commissioners were not officers because the "mere power to investigate some particular subject and report thereon . . . does not constitute a person an officer").

And while SSA ALJs exercise discretion and independent judgment in determining eligibility for benefits and adjudicating other issues they are tasked to decide, they do so with the benefit of comprehensive agency guidelines, such as medical-vocational grids, that provide detailed schedules on medical criteria for different levels of impairment. SSA also provides internal guidance tools, like the Hearings, Appeals and Litigation Law (HALLEX) manual, intended to "communicate[] guiding principles and procedures" to SSA adjudicators. HALLEX I-1-0-3. One of these guidelines even urges ALJs to refer novel policy issues to their agency supervisors, rather than decide the question themselves in the first instance, while recognizing that the need for any referral will be

rare given the comprehensive guidelines already provided.[10]

SEC ALJs, although also circumscribed by APA and agency constraints in their policy-making role, have considerably more leeway for interstitial common-law decision-making. In contrast to non-adversarial determinations of benefit eligibility status, administrative enforcement proceedings will, by necessity, involve the refining of "statutory standards" through "case-by-case evolution." *SEC v. Chenery Corp*, 332 U.S. 194, 202-03 (1947). Here, at least by Petitioner's account, the ALJ's definition of "backtest" helped shape the course of the litigation. *See* Pet. Br. 7-8. While ultimately it is the Commission's final call, the opportunity for SEC ALJs to make these sorts of legal determinations even in the first instance is foreign to SSA ALJs, given the detailed agency policies and guidelines that cabin their discretion.

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[10] *See* HALLEX I-2-1090. HALLEX guidelines are not promulgated through notice and comment rulemaking and courts have recognized that they are not binding. *See Schweiker v. Hanson*, 450 U.S. 785, 789 (1981); *Moore v. Apfel*, 216 F.3d 864, 868-69 (9th Cir. 2000). The extent to which HALLEX guidelines bind SSA ALJs—particularly if they encroach upon an ALJ's independence in how hearings are conducted or may conflict with published regulations—is frequently litigated between AALJ members and SSA. The agency's position is that HALLEX is binding on all SSA employees, including ALJs. Whatever the propriety of the agency's position, it further supports the conclusion that its ALJs are federal employees, albeit sui generis employees who conduct due process hearings pursuant to the APA with concomitant quasi-judicial decision-making powers.

b. An additional distinguishing feature of the scope of authority exercised by SSA ALJs as compared to others is the nature of internal review mechanisms. In contrast to other agencies, the Appeals Council plays a critical role. *See generally* 20 C.F.R. §§ 404.900-.996, 422.205; *see also Mullen v. Bowen*, 800 F.2d 535, 536-37 (6th Cir. 1986) (en banc) (describing Appeals Council). Not only must claimants dissatisfied with an ALJ determination seek Appeals Council review to exhaust administrative remedies, 20 C.F.R. §§ 404.967, 416.1467, but the Council itself can (and often does), on case-specific own-motion review, review ALJ decisions *sua sponte*. *See id.* § 404.969(a).[11] In addition, as part of a more generalized quality review system, the agency selects a sampling of cases to review pre-effectuation. *See id.* §§ 404.969(b), 416.1469(b).

To preserve ALJ independence, SSA regulations bar the agency from conducting pre-effectuation reviews of ALJs' decisions based on the identity of a specific ALJ or the hearing office where the decision was made. 20 C.F.R. §§ 404.969(b)(1), 416.1469(b)(1). Instead, SSA uses random and selective sampling to pick decisions allowing benefits for such reviews. *Id.* The agency also undertakes special studies based on anomalies identified. *See generally* SSA, Office of Inspector General, Congressional Response Report,

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[11] Further support for recognizing that SSA ALJs are federal employees, not officers, is the fact that their decisions can be overturned by an Appeals Council staffed by employee attorney-advisors, who are exercising the Commissioner's delegated final decision-making authority.

The Social Security Administration's Review of Administrative Law Judges' Decisions, No. A-07-12-21234, at 6-7 (March 2012).[12] Through these various review processes, the SSA aims to ensure that ALJ decisions, overall, do not stray from mandated regulatory policy.

c. There is a rationale behind these constraints. This Court, nearly a half-century ago, recognized that the disability programs administered by SSA are of "a size and extent difficult to comprehend." *Richardson*, 402 U.S. at 399. And the workload has only grown since then. The number of ALJs employed by SSA, and the sheer quantity of cases they handle, is further indication that SSA ALJs are usually applying policies, not making them.

There are only five ALJs at the SEC, and the Federal Trade Commission and the Consumer Finance Protection Bureau, other agencies that pursue administrative enforcement actions, have only one apiece. *See* OPM, ALJs by Agency.[13] In contrast, some 1700 ALJs currently serve at the Social Security Administration. *See supra* note 2. And they handle a far greater number of cases, both overall and per judge.

During the first five months of fiscal year 2018, roughly 283,000 initial decisions were issued by SSA ALJs.[14] And although ALJs succeeded in reducing the

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[12] *Available at* https://goo.gl/8QDVfK.

[13] *Available at* https://goo.gl/Vf8UV4.

[14] *See* https://goo.gl/vhfLJA.

agency's backlog during this period, nearly 1,000,000 cases remain pending. *Id.* In contrast, fewer than 500 administrative proceedings are currently pending, at all stages, before the SEC.[18]

Management challenges for a hearing load of this magnitude have yielded the unique agency appeal structure and system of internal review described above. The agency has long "sought to balance the need for accuracy and fairness to the claimant with the need to handle a large volume of claims in an expeditious manner." Astrue Testimony, *supra*, at 3. The Social Security hearings system "must be fair—and it must work." *Richardson*, 402 U.S. at 399.

These twin goals are sometimes competing, reflecting a tension between the promise of individualized justice and a "need for efficiency" that is "self-evident." *Heckler*, 461 U.S. at 461 n.2. For years, "SSA and its independent-minded ALJs [have been] locked in a continuing struggle over the proper parameters of . . . management standards." Paul R. Verkuil, *Reflections upon the Federal Administrative Judiciary*, 39 U.C.L.A L. REV. 1341, 1354 (1992). And *Amicus* AALJ has long fought to protect ALJ independence in setting the right balance. *See, e.g.*, *Ass'n of Admin. Law Judges v. Heckler*, 594 F. Supp. 1132, 1143 (D.D.C. 1984) (recognizing that focusing review on ALJs with high allowance rates created an "atmosphere of tension and unfairness which violated the spirit of the APA, if no specific provision thereof"); *Ass'n of Admin. Law*

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[18] *See* https://goo.gl/E9xMFY.

Judges v. Colvin, 777 F.3d 402 (7th Cir. 2015); *see also id.* at 406 (Ripple, J., concurring) (declining to assert jurisdiction over AALJ's challenge to SSA policy mandating number of cases to be decided annually and recognizing the "gnarled intersection" of the APA and the Civil Service Reform Act).

This ongoing tug-of-war reflects how SSA ALJs are subject to more levels and varieties of internal agency control than are their counterparts in other agencies. Such a high degree of agency review and supervision is yet another feature distinguishing them from SEC ALJs.

2. The nature of SSA ALJs' working conditions confirms they are federal employees. And they have long been classified as such by OPM, unionized as federal employees, and represented by AALJ under the Federal Service Labor-Management Relations Statute (FSLMRS), 5 U.S.C. §§ 7101 *et seq.*

Ultimately, whatever this Court decides about the constitutional officer status of SSA or other ALJs, it should have no bearing on their status as federal employees protected under federal labor laws. The Constitution has nothing to say about employee status under federal labor statutes, so even if deemed constitutional officers, ALJs can and should still be treated as employees under the relevant federal statutes. *Cf. Free Enterprise Fund*, 561 U.S. at 485-86 (noting provisions that Board members are not government officials for statutory purposes, but

parties' agreement that members are officers of the United States for constitutional purposes).

To start, and *contra* Pet. Br. 35-36, the APA uses the terms officers and employees interchangeably when describing ALJs. The statute that created ALJs thus "consistently uses the term 'officer' or the term 'officer, employee, or agent'" to "refer to [agency] staff members." Kenneth Culp Davis, *Separation of Functions in Administrative Agencies*, 61 HARV. L. REV. 612, 615 & n.11 (1948). But reference to simple "officers," rather than "officers of the United States" does not establish congressional intent to create an office. *See* Court-Appointed *Amicus* Br. 55. And in 1966, when Congress enacted title 5 into positive law, it replaced the term "officer" with the term "employee." *E.g.*, 5 U.S.C. § 554(d) (referencing "the employee who presides at the reception of evidence" under § 556, who "shall make the recommended decision or initial decision required by § 557"); *see* Court-Appointed *Amicus* Br. 55-56. This Court too, in its pathmarking decision on the protections afforded to hearing examiners under the APA, has used the terms officer and employee interchangeably. *Ramspeck*, 345 U.S. at 132.

What's more, the Government's decades-long unbroken course of conduct in engaging in collective bargaining with *Amicus* AALJ confirms that ALJs are protected federal employees under the FSLMRS. That statute defines employee as "an individual employed in an agency." 5 U.S.C. § 7103(a)(2)(A). And the definition of "professional employees," in 5 U.S.C. § 7103(a)(15),

readily encompasses ALJs, who regularly, and exclusively, make "determinations that require judgment and extensive educational background, the hallmark of professional employees." *U.S. Dep't of Homeland Sec., Bureau of Customs & Border Prot.*, 61 FLRA 485, 493 (2006). Although SSA ALJs' status as federal employees for collective bargaining purposes would not preclude inferior officer status under Article II, it is more consistent to consider ALJs employees in both contexts.

In sum, any Article II holding for SEC ALJs cannot resolve the constitutional status of ALJs in other agencies. And whatever the constitutional result, it is irrelevant to the question of whether ALJs are protected federal employees under the FSLMRS.

III. This Court Should Not Reach The Removal Question, But The APA Provisions Regarding Removal Are Constitutional.

A. The Removal Question Is Not Presented.

The Government alone asks this Court to apply the constitutional avoidance canon to reinvent the APA's "good cause" removal provision, 5 U.S.C. § 7521, because "[i]f Section 7521 were [not] construed" that way, it might "undermine the President's ability to supervise the actions of the Executive Branch" to an unconstitutional degree. U.S. Br. 48. There is no reason to reach this hypothetical question, and every reason not to.

First, the question was not pressed or passed on below, which is reason enough not to decide it here. *See, e.g.*, *United States v. United Foods, Inc.*, 533 U.S. 405, 417 (2001).[16] Second, there is no circuit law on the constitutional validity of the good cause removal standard for ALJs, much less a circuit split. Finally, the question is not only "not presented" here (Pet. Br. 38), it is a hypothetical that might not be presented at all. The Government does not argue that the APA is unconstitutional as written, but only that it *might* be unconstitutional *if* it were not construed to permit ALJ removal for misconduct, poor job performance, and failure to follow agency rules—even as the Government concedes that some ALJs *have* been removed on those grounds. *See* U.S. Br. 46.

Ultimately, the question of officer status under the Appointments Clause is entirely distinct from the question of how much Executive Branch supervision is enough under the Take Care Clause. There is thus no compelling reason for the Court to cast its long-established practice aside and to decide the removal question.

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[16] The Government usually agrees, even in cases raising the same separation of powers concerns. *See* Br. for United States in Opposition to Certiorari, *Scott v. FDIC*, No. 17-567, at 5-6 (arguing the Court should not review whether FDIC ALJs are inferior officers because the question was not pressed or passed upon below).

B. The APA Removal Provision Is Constitutional Because ALJs Perform Quasi-Judicial Functions and the APA Permits Sufficient Executive Control.

If the Court reaches the question, it should hold that the APA's ALJ-removal provision is constitutional. Even if ALJs are inferior officers, the careful balance achieved by Congress in the APA between political accountability and impartiality is entirely consistent with the Constitution and protects the Executive's authority and responsibility under the Take Care Clause.

1. At the outset, long-settled administrative practice and the very deliberate choices made by Congress to secure impartial administrative adjudications create a high bar for any claim that ALJ removal protections unconstitutionally impede the Executive's ability to "take Care that the Laws be faithfully executed," U.S. Const., Art. II, § 3.

The APA is, of course, a statute that comes to the Court with a presumption of constitutionality. *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 44 n.9 (1983) (describing the "presumption of constitutionality afforded legislation drafted by Congress"). And limiting the grounds for removal of ALJs is a "'[l]ong settled and established practice'" since 1946, which "'is a consideration of great weight in a proper interpretation of constitutional provisions' regulating the relationship between Congress and the President." *NLRB v. Noel Canning*, 134 S. Ct. 2550, 2559 (2014) (alteration in

original) (quoting *The Pocket Veto Case*, 279 U.S. 655, 689 (1929)); *see id.* at 2560 (citing with approval the reliance of *Dames & Moore v. Regan*, 453 U.S. 654, 686 (1981), on one branch's acquiescence in a practice since 1952).

That long-settled practice carries added force here given the extensive study and deliberation undertaken by Congress in enacting the APA and resolving the pre-APA problem of unwarranted pro-agency bias in agency decision-making while ensuring plenary agency control over administrative policymaking. *See* pp. 6-7, *supra*; Pierce Br. 6-11; Forum Br. 4-9; FALJC Br. 4-7. AALJ joins those *amici* in urging that Congress's solution to the problems that plagued pre-APA administrative decision-making should not be overturned lightly, particularly when the proposed "solution" of increasing the power of agency heads over ALJ tenure could introduce the very bias that the APA was enacted to eradicate. *See, e.g.*, Pierce Br. 19-21; Forum Br. 20-21.

2. The Take Care Clause demands no such upending of congressional imperatives, even if ALJs are deemed inferior officers. As has been long established, and was recently reiterated in *Free Enterprise Fund*, Congress can, consistent with the Take Care Clause, choose to substantially limit the authority of the Executive Branch to remove officers, particularly for (i) inferior officers and (ii) officers exercising quasi-judicial authority. 561 U.S. at 492-94.

Congressional authority to limit the Executive's removal authority is thus at its zenith here, where both criteria are satisfied, and then some. If officers at all, ALJs are inferior officers who exercise quasi-judicial power. They are also subject to full "good cause" removal and other levers of executive supervision. Unsurprisingly, even as the Court in *Free Enterprise Fund* concluded that the Constitution, in unique circumstances, bars a combination of removal limits on principal and inferior officers, it recognized that ALJs are different because of their adjudicative function. 561 U.S. at 506-07, 507 n.10 ("[U]nlike members of the Board, many administrative law judges of course perform adjudicative rather than enforcement or policymaking functions, *see* §§ 554(d), 3105, or possess purely recommendatory powers."). That recognition presages the correct holding here—that the APA's ALJ-removal provision does not unconstitutionally trench on executive power.

a. Inferior officer classification casts no constitutional doubt on statutes restricting the President's (or relevant principal officer's) removal authority. The power to remove is not expressly conveyed in the Appointments Clause and may be limited by Congress so long as the limitations do not impede the President's power and duty under the Take Care Clause. *See, e.g.*, *Free Enterprise Fund*, 561 U.S. at 492-94. And it is well established that, with respect to inferior officers, Congress "'may limit and restrict the power of removal as it deems best for the public

interest.'" *Id.* at 494 (quoting *United States v. Perkins*, 116 U.S. 483, 485 (1886)).

What's more, even for *principal* officers, the President's removal authority may be limited to good cause when the officers exercise quasi-judicial authority, intended by Congress to operate with some independence from the Executive. *See Free Enterprise Fund*, 561 U.S. at 493 (because the FTC was "'quasi-legislative and quasi-judicial' rather than 'purely executive,' and . . . Congress could require it 'to act . . . independently of executive control,'" Congress could limit removal to good cause) (quoting *Humphrey's Executor v. United States*, 295 U.S. 602, 627-29 (1935)).

b. For ALJs, these two attributes—quasi-judicial power and subordinate status—are combined, maximizing Congress's power to shield ALJs from executive removal in furtherance of impartial decision-making. The APA's ALJ-removal provision satisfies the Take Care Clause given the adjudicative function of ALJs, the supervisory mechanism of good cause removal itself (including the involvement of the Merit Systems Protection Board (MSPB)), and the other levers of executive supervision over ALJ decisions under the APA.

First, ALJs fit comfortably within the recognized principle that Congress can limit the ability to remove quasi-judicial officers to serve the public interest in adjudicative impartiality. In *Wiener v. United States*, 357 U.S. 349 (1958), the Court considered whether the President could remove commissioners at will when

Congress established a Commission to adjudicate certain war claims "according to law." *Id.* at 349–51. Holding that the President could not do so, the Court found "the intrinsic judicial character of the task with which the Commission was charged" dispositive, because it indicated the body was intended to be "'entirely free from the control or coercive influence, direct or indirect,' of either the Executive or the Congress." *Id.* at 355–56 (quoting *Humphrey's Executor*, 295 U.S. at 629). The Court held that Congress's evident design to render the Commission impartial meant that "Congress did not wish to have hang over the Commission the Damocles' sword of [at will] removal." *Id.* at 356.

Like the commissioners in *Wiener*, ALJs address issues "to be 'adjudicated according to law,' that is, on the merits of each claim, supported by evidence and governing legal considerations," *id.* at 355, evidencing the "intrinsic judicial character" of the ALJs' task. Moreover, ALJs perform quasi-judicial tasks alone, not a mix of adjudicative, policymaking, and enforcement functions (unlike the Board in *Free Enterprise Fund*, 561 U.S. at 485-86). They are bound by executive policies embodied in rules and are prohibited under the APA from taking part in any agency investigation and enforcement functions, 5 U.S.C. § 554(d).

And, as in *Wiener*—arguably even more so, because the APA expressly addresses ALJ removal—Congress plainly intended to insulate ALJs from at-will removal in order to promote the adjudicative impartiality that it deemed necessary to serve the

public interest. Congress made the well-studied decision that ALJs could not act with sufficient impartiality if the "Damocles sword of removal" hung over their heads—while retaining executive accountability through the agency's ability to replace or negate any ALJ decision.

Second, the good cause removal provision provides ample executive supervisory authority and satisfies constitutional minimums, notwithstanding the role of the MSPB. Even with respect to a "purely executive" officer, the authority to remove for good cause is an important means of "supervising or controlling" an officer, and limiting removal to "good cause" does not "unduly trammel[ ] on executive authority." *Morrison v. Olson*, 487 U.S. 654, 690-91, 696 (1988). *A fortiori*, it satisfies the Take Care Clause for quasi-judicial officers like ALJs.

The APA does not limit the ordinary "good cause" standard in any way, unlike the removal standard at issue in *Free Enterprise Fund*, which allowed Board members' removal only upon a showing of "willful violations . . . willful abuse of authority; or unreasonable failure to enforce compliance." 561 U.S. at 503. And, contrary to the Government's suppositions (U.S. Br. 46-47), the removal of ALJs for a variety of reasons confirms that "ordinary" good cause applies. Among other things, ALJs have been removed (sometimes over AALJ's protest) for being absent for extended periods, declining to set hearing dates, having a high rate of significant adjudicatory errors, not following mandatory rules, and deciding too few

cases. *See* U.S. Br. 46; Forum Br. 22; Harold J. Krent, *Presidential Control of Adjudication Within the Executive Branch*, 65 CASE W. RESERVE L. REV. 1083, 1109 & nn. 134-36 (2015); Kent H. Barnett, *Resolving the ALJ Quandary*, 66 VAND. L. REV. 797, 807 (2013); *see also e.g.*, *Shapiro v. Soc. Sec. Admin.*, 800 F.3d 1332 (Fed. Cir. 2015); *Abrams v. Soc. Sec. Admin.*, 703 F.3d 538 (Fed. Cir. 2012). Good cause removal thus remains an important and powerful tool of executive accountability, without the interpretive gloss the Government urges.[17]

Furthermore, the role of the MSPB as a neutral arbiter of good cause does not unconstitutionally attenuate executive control, nor create the same kind of "dual for-cause limitations on . . . removal" at issue in *Free Enterprise Fund*, 561 U.S. at 492, even though there are limits on the President's ability to remove the members of the MSPB, 5 U.S.C. § 1202(d).[18] The agency,

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[17] Outside of litigation, the Executive Branch recognizes that a congressional amendment, not a judicial re-interpretation, is required to meaningfully alter the APA's removal provision for ALJs. The Social Security Administration has sought, in its fiscal year 2019 budget, an amendment to the APA that would, among other things, create "probationary periods for newly hired ALJs" and "allow the faster removal of ALJs." Social Security Administration, *Fiscal Year 2019 Budget Overview*, at 28, https://goo.gl/WKCAKJ.

[18] The constitutionality of the APA's ALJ removal provision likewise does not depend on the happenstance of whether an ALJ is assigned to an agency headed by an officer who can be removed by the President at will, or not. Even the Government's argument does not turn on whether "the Department Head is permissibly insulated from presidential removal at will." U.S. Br. 52 n.8. Given that ALJs are fungible across agencies under the APA, *see* p. 10,

not the MSPB, decides if there is good cause to remove an ALJ and initiates a removal. 5 U.S.C. § 7521(a) ("An action may be taken against an administrative law judge . . . by the agency in which the administrative law judge is employed. . . ."). That the agency must prove good cause to the MSPB, *id.*, is akin to judicial review, which is constitutional (*e.g.*, *Morrison*, 487 U.S. at 686), even though the Executive lacks authority to remove Article III judges.[19]

Finally, the limited nature of ALJ authority and the additional tools of executive supervision must be factored into the calculus of whether the Executive Branch exercises sufficient supervision over ALJs. *See Morrison*, 487 U.S. at 696 (holding that executive supervision of an independent counsel was constitutionally sufficient when, *inter alia*, the counsel's jurisdiction was defined and limited and the governing statute "requires that the counsel abide by Justice Department policy unless it is not 'possible' to do so"). ALJs, too, are bound by agency policy, and there are many other executive supervisory tools available—including the agency's authority to completely replace each and every one of

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supra, it would be odd if the constitutionality of their tenure protections waxed and waned with each different agency assignment.

[19] In objecting to the MSPB's role, the Government would permit the MSPB to find facts, yet be bound by the agency's position that the asserted facts are "good cause." U.S. Br. 52. Such an interpretation—under which "good cause" means nothing more than requiring proof of whatever facts the agency decided justified removal—would render the concept of "good cause" meaningless and cannot be squared with the APA.

the ALJ's decisions that it disagrees with. This substantive control provides complete accountability within the Executive Branch for any decision issued by an ALJ.

In sum, far from being a recent and unprecedented innovation, *see Free Enterprise Fund*, 561 U.S. at 505-06 (stressing the "lack of historical precedent" in holding particularly restrictive dual for-cause removal limitations unconstitutional), the practice of limiting ALJ removal to good cause (as proved to the MSPB) has a settled historical pedigree and falls within a long line of precedents recognizing the authority of Congress to limit removal authority for quasi-judicial officials like ALJs to foster the adjudicative impartiality that Congress has judged critical to the public interest. *See* 5 U.S.C. § 556(b). Good cause removal, coupled with plenary agency control over ALJ decisions, safeguards the Executive's authority to faithfully execute not only the laws governing the matters under decision, but also the APA's guarantees of an impartial hearing officer and procedural fairness.

CONCLUSION

For the foregoing reasons, the decision below should be affirmed; this Court should clarify that any ruling with respect to SEC ALJs does not extend to ALJs from other agencies; and should likewise confirm, if it reaches the removal question at all, that current ALJ removal protections are constitutionally sound.

Respectfully submitted,

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No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, ET AL.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF FOR THE CATO INSTITUTE AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Can an executive agency's officers investigate, prosecute, and adjudicate disputes without oversight from the chief executive?

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INTEREST OF THE *AMICUS CURIAE*[1]

The Cato Institute was established in 1977 as a nonpartisan public policy research foundation dedicated to advancing the principles of individual liberty, free markets, and limited government. Cato's Robert A. Levy Center for Constitutional Studies was established in 1989 to promote the principles of limited constitutional government that are the foundation of liberty. Toward those ends, Cato publishes books and studies, conducts conferences, issues the annual *Cato Supreme Court Review*, and files *amicus* briefs.

This case is important to Cato because it concerns core separation-of-powers issues and the democratic accountability of executive officers.

INTRODUCTION AND SUMMARY OF ARGUMENT

The Constitution created three branches of government. The legislative and executive branches are controlled by the electorate. The president is vested with all executive power, and therefore controls the executive branch. 1 Annals of Cong. 481 (James Madison, June 16, 1789) ("[I]f any power whatsoever is in its nature executive, it is the power of appointing, overseeing, and *controlling* those who execute the laws.") (emphasis added). The president has a duty to see that the law is faithfully executed. To do this he must be able to remove those officers who fail in their duties.

And yet, the SEC's administrative law judges (ALJs) are protected from control by the electorate.

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[1] Rule 37 statement: All parties lodged a blanket consent with the Clerk. No party's counsel authored any of this brief. No person other than *amicus* funded its preparation and submission.

The president lacks the ability to remove ALJs should they abuse their powers or fail to use their discretion to act intelligently or wisely.

The D.C. Circuit ruled that ALJs need not be subject to presidential removal because they are not executive officers. When the case was reheard *en banc*, the court deadlocked 5–5, leaving in place the panel's earlier characterization of ALJs as something less than the category of officers subject to the removal power. But ALJs' duties are similar to Special Trial Judges (STJs) and court clerks, positions the Court has previously determined to be officers. If anything, ALJs have more power and exercise their duties with greater discretion and independence than STJs or court clerks.

The similarities between ALJs and court clerks or STJs are alone enough to show that ALJs are officers. Even more, ALJs fit the definitions of an "executive officer" established by legal and historical precedent. Chief Justice John Marshall articulated a test for distinguishing an officer from an employee. In *United States v. Maurice*, 26 F. Cas. 1211 (C.C.D. Va. 1823), he explained that if a position did not require a contract because the government had prescribed duties of the position independent of a specific position-holder—and that successive holders' duties would not change—then that position is an office, and thereby its holder an officer. The Court later expanded on Marshall's criterion by setting parameters for the tenure, duration, compensation, and duties of an officer. Parameters that distinguish an officer from an employee. Evaluating the ALJ role against these parameters demonstrates that ALJs are officers, not employees. Most im-

portantly, ALJs have significant discretion and perform more than ministerial duties, which, based on the Court's definitions, makes them ALJs officers.

Both Congress and the SEC have recognized that ALJs are officers. Considering how much more closely the ALJ position aligns with the definition of an officer than that of an employee, this should not be a surprise.

The quasi-judicial nature of an ALJ's role does not change their status as officers. The Court established that presidential accountability applies to officers with a quasi-judicial function over 90 years ago. It held that, even for a quasi-judicial executive officer, the president "may consider the decision after its rendition as a reason for removing the officer, on the ground that the discretion regularly entrusted to that officer by statute has not been on the whole intelligently or wisely exercised." *Myers v. United States*, 272 U.S. 52, 135 (1926). Precedent going back to the Founding also supports the notion that SEC ALJs must be subject to executive oversight. The Comptroller of the Treasury was then considered quasi-judicial for the same reasons an ALJ should be so considered today, yet still removable by the president. The president has also removed territorial judges, demonstrating that the judicial character of an executive-branch officer does not change the president's authority to remove that officer.

This case presents an important application of the Appointments Clause. Accepting arguments like those presented here, the Tenth Circuit rightly concluded that ALJs are officers in *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016). The Court should similarly hold that ALJs are officers who must be appointed in accordance with Article II, ensuring proper accountability and adherence to basic constitutional principles.

ARGUMENT

I. SEC ALJS ARE EXECUTIVE OFFICERS BECAUSE OF THEIR DISCRETION AND POWER

ALJs are officers, not employees, because of the discretion they wield and the power they exercise. The close similarities between ALJs and STJs or court clerks—positions that the Court has deemed to be offices—are sufficient proof that ALJs are officers. Moreover, ALJs fit multiple legal and historical definitions of officers. On this, the D.C. Circuit erred.

A. ALJs Have Duties and Powers Similar to Other Positions That the Court Has Held to Be Offices

ALJs perform many important functions, including, critically, shaping the evidentiary record, evaluating witness credibility, and rendering decisions and findings of fact after contested trial-like proceedings. 17 C.F.R. §201.111. These factors alone are more than enough to render them officers, as *Freytag v. C.I.R.* makes abundantly clear 501 U.S. 868 (1991).

In *Freytag*, the Court determined that STJs are executive officers because of their discretion and power. *Id.* at 881-82. There is no material difference between the discretion and power STJs and SEC ALJs exercise. Like the *Freytag* STJs, SEC ALJs "perform more than ministerial tasks." *Id.* at 881. They too "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders." *Id.* at 881-82; 17 C.F.R. §201.111. And, like STJs, ALJs "exercise significant discretion in the course of carrying out their duties." *Freytag*, 501 U.S. at 881-82; 17 C.F.R. §201.111. ALJs notably use

their discretion to make findings as to the credibility of witnesses and the SEC defers to ALJs' "credibility finding, absent overwhelming evidence to the contrary." *In re Clawson*, Exchange Act Release No. 48143, 2003 WL 21539920, at *2 (July 9, 2003); *In re Pelosi*, Securities Act Release No. 3805, 2014 WL 1247415, at *2 (Mar. 27, 2014) ("The Commission gives considerable weight to the credibility determination of a law judge since it is based on hearing the witnesses' testimony and observing their demeanor. Such determinations can be overcome only where the record contains substantial evidence for doing so."); *Universal Camera Corp. v. N.L.R.B.*, 340 U.S. 474, 496 (1951). Moreover, the opinions ALJs issue are final unless appealed and *Freytag* emphasized the importance of STJs' power to issue opinions. 5 U.S.C. § 557(b); *Freytag*, 501 U.S. at 882 (noting that the fact that the STJ can "render the decisions of the Tax Court" in some cases is enough to be considered an officer).

The ALJs' authority also mirrors that of court clerks, which, under the Court's determination, rendered them officers. *See Ex parte Hennen*, 38 U.S. 230, 260 (1839) ("These clerks fall under that class of inferior officers, the appointment of which the Constitution authorizes Congress to vest in the head of the department."). This despite the fact that clerks have no power to make final decisions for the court outside of default judgments (which can be rescinded by the court). FRCP 77(2); FRCP 55(b)(1)—as can ALJs, 17 C.F.R. § 201.155, who can also reject deficient filings as some clerks can, 17 C.F.R. § 201.180 (b), (c). Clerks can administer oaths and affirmations, 28 U.S.C. § 953, as can ALJs. 17 CFR 201.111(a). There is no power or discretion that clerks have that ALJs do not.

Since these powers make a clerk an "officer of the United States," they have the same effect on ALJs.

The panel below ruled that SEC ALJs are not officers because their decisions are not final (in that they are appealable to the Commission). *Raymond J. Lucia Cos., Inc. v. SEC*, 832 F. 3d 277, 285 (D.C. Cir. 2016). This argument fails in the face of respondents' actual experience appearing before SEC ALJs. Although ALJs' rulings on questions of law are subject to review, their findings of fact are nearly unassailable and are given great deference by the Commission. That is, of course, assuming that a respondent proceeds so far as to obtain an appealable decision. As many as half of SEC enforcement actions result in settlement with up to 80 percent of those settlements being concluded during administrative proceedings. Urska Velikonja, *Securities Settlements in the Shadows*, 126 Yale L.J. Forum 124 (2016). The tenor of administrative proceedings, set in the SEC almost exclusively by the ALJs, inform both respondents' decisions and their counsels' admonitions regarding the wisdom of settlement. If most respondents never make their case before the Commission and if those who do are almost irretrievably bound by the factual determinations of ALJs, it is difficult to see how the existence of such limited review can be controlling. If it is true that "[w]ise observers have long understood that the appearance of justice is as important as its reality," it must also be true that appearance of justice does not trump actual injustice in practice. *J.E.B. v. Ala. ex rel. T.B.*, 511 U.S. 127, 161 n.3 (1994) (Scalia, J., joined by Rehnquist, C. J., and Thomas, J., dissenting).

B. SEC ALJs Fit Legal Precedents and Historical Definitions of Officers

There are also important historical precedents for considering ALJs to be officers. At the Founding, jurists understood that a position's holder must be an officer if executing the duties of that position entailed exercising coercive authority over others. "It is a rule, that where one man hath to do with another's affairs against his will, without his leave, that is an office, and he who is in it, an officer." Giles Jacob, A New Law Dictionary 641 (10th ed. 1773).

The first Supreme Court justice to consider the characteristics that distinguish officers from employees was Chief Justice John Marshall, in *United States v. Maurice*, 26 F. Cas. 1211 (C.C.D. Va. 1823). That case required the Court to determine if an agent for fortifications was an officer of the United States. The opinion in that case established general criteria for determining whether a position is or is not an office:

> An office is defined to be "a public charge or employment," and he who performs the duties of the office, is an officer. If employed on the part of the United States, he is an officer of the United States. Although an office is "an employment," it does not follow that every employment is an office. A man may certainly be employed under a contract, express or implied, to do an act, or perform a service, without becoming an officer. But if a duty be a continuing one, which is defined by rules prescribed by the government, and not by contract, which an individual is appointed by government to perform, who enters on the duties appertaining to his station, without any contract defining them, if those duties continue, though the person be changed; it seems very difficult to distinguish such a

> charge or employment from an office, or the person who performs the duties from an officer.

Id. at 1214.

To Marshall, it was the lack of a contract to perform a service in which different people may consecutively hold the same position that distinguishes an "office" from employment. *Maurice*, 26 F. Cas. at 1214. The Court cited Marshall's definition of an office in a later case regarding the status of a merchant appraiser. *Auffmordt v. Hedden*, 137 U.S. 310, 327 (1890). Marshall's definition applies to an SEC ALJ, who is not under contract to perform a service but rather "enters on the duties appertaining to his [or her] station" and that "those duties continue, though the person be changed." The criteria the Court applied in *Auffmordt* provides even more support for classifying SEC ALJs as the officers they are. *See Id.* 5 U.S.C. § 3105.

In *United States v. Hartwell*, the Court issued another, more comprehensive definition of "office," which ALJs fit absolutely. 73 U.S. 385 (1867). "[A]n office is a public station, or employment, conferred by the appointment of government" and "[t]he term embraces the ideas of tenure, duration, emolument, and duties." *Id.* at 393. The Court applied these requirements and found that n officer is someone "appointed pursuant to law, and his compensation was fixed by law." *Id.* An ALJ is likewise appointed pursuant to law and the compensation is fixed by law. 5 U.S.C. § 3105; 5 U.S.C. § 5372. The Court then noted that "[v]acating the office of his superior would not have affected the tenure of his place," *Hartwell*, 73 U.S. at 393, underlining the independent nature of an office. An ALJ's tenure is likewise unaffected by the removal of another person

from office. Finally, the Court recognized that an officer's "duties were continuing and permanent, not occasional or temporary," *id.*, accurately describing an ALJ's duties. 5 U.S.C. § 7521.

The Court expanded on that definition to require that one must be "exercising significant authority" to be considered an officer. *Buckley v. Valeo*, 424 U.S. 1, 126 (1976). This expansion was not meant to challenge prior understandings of officer status, but to crystalize the reasoning that led the Court to determine district court clerks and postmasters first class to be inferior officers. *Id. Buckley's* definition of officer included "all appointed officials exercising responsibility under the public laws of the Nation." *Id.* at 131. The panel's reliance on *Buckley* was thus misplaced.

In *Buckley*, the Court distinguished employees from officers by describing them as "lesser functionaries subordinate to officers of the United States." *Id.* The Court's decision in *Freytag* reflected this distinction, as it determined that special trial judges are officers because they "perform more than ministerial tasks" and exercise "significant discretion." *Freytag*, 501 U.S. at 881-82. *Buckley's* emphasis on the relative independence of a position and its organizational relationship to other officers closely pertains to SEC ALJs. The statutory framework governing the authority of ALJs ensures that they are not directly controlled by any other officer. 5 U.S.C. § 7521(a).

Considering the independence of and discretion wielded by the SEC's ALJs in the context of relevant historical and legal precedents, it is clear why Congress considers ALJs to be officers. The SEC's enabling statute provides that ALJs' authority to hold hearings is predicated upon their status as officers. 15 U.S.C. §

77u ("All hearings shall be public and may be held before the Commission or an *officer or officers* of the Commission designated by it.") (emphasis added); *see also* 17 C.F.R. § 201.111 (SEC regulation referring to an ALJ as a "hearing officer").

II. ADMINISTRATIVE LAW JUDGES' PROTECTION FROM REMOVAL IS UNCONSTITUTIONAL UNDER THE APPOINTMENTS CLAUSE

The Constitution guarantees that even officers who are appointed (not elected) are nonetheless accountable to the people. Although the Constitution offers no explicit guidance on removals, jurists have understood that removals "empower the President to keep these officers accountable" including through the removal of the officers if necessary. *Free Enter. Fund v. Pub. Co. Acc'ting Oversight Bd.*, 561 U.S. 477, 483 (2010).

A. ALJs Must Be Removable by the President to Ensure Democratic Accountability for Executive Officers

Since the Founding, jurists have understood that the president, to fulfill his constitutional duty to ensure that the laws be faithfully executed, must have the power to remove executive officers. The Constitution does not specify how an officer can be removed (other than impeachment), and so a debate occurred in the First Congress over the presidential power to remove officers. Some felt that impeachment was the only proper method of removal because it was the only one specifically mentioned. James Madison disagreed, declaring that "it is absolutely necessary that the President should have the power of removing from office; it will make him, in a peculiar manner, responsible for

their conduct, and subject him to impeachment himself, if he suffers them to perpetrate with impunity high crimes or misdemeanors against the United States, or neglects to superintend their conduct, so as to check their excesses." 1 Annals of Congress 387 (1789). Such a power to remove officers was seen at the time as "incident to the power of appointment." *Myers*, 272 U.S. at 110 (1926).

Madison did not consider this power to remove to be absolute, but "because Congress may establish offices by law," Congress could decide if the officer's tenure was "either during good behavior or during pleasure." 1 Annals of Congress 389 (1789). In the end of the debate, the First Congress by a "considerable majority" resolved "the power of removal to be in the President." *Id.* at 399.

Despite Congress's authority to grant tenure for good behavior, as of 1903 "no civil officer [had] ever held office by a life tenure since the foundation of the government" with the exception of Article III judges. *Shurtleff v. United States*, 189 U.S. 311, 316 (1903). When Congress attempted to condition the removal of a postmaster on congressional approval, the Court held that to be an unconstitutional limitation on the power of the president. *Myers*, 272 U.S. at 176.

If a limitation on the president's removal power is unconstitutional, it is immaterial which entity exercises the limitation. If it is unconstitutional to condition the president's removal power on the Senate's consent, it is equally unconstitutional to condition the removal power on the consent of the Merit Systems Protection Board (MSPB). As Madison said, if the executive officer "shall not be displaced but by and with the advice and consent of the senate, the President is no

longer answerable for the conduct of the officer; all will depend on the senate. You here destroy a real responsibility without obtaining even the shadow." 1 Annals of Congress 394-95. Likewise, the president is not fully answerable for the conduct of ALJs who cannot be removed without the advice and consent of the MSPB (which also cannot be removed but for cause). When an ALJ goes beyond the powers of that office, but the MSPB refuses to exercise its removal power, which elected official are the American people to blame?

B. SEC ALJs Are Not Democratically Accountable, Because Their Removal Involves Two Layers of Protection

SEC ALJs are inferior officers that are protected from presidential removal by at least two layers of for-cause removal protection. Permitting an executive officer to enjoy such insulation from removal unconstitutionally prevents the president from exercising the necessary control to be politically accountable for the actions of the officer. *Free Enter. Fund*, 561 U.S. at 477.

The first layer of protection exists at the SEC level. The SEC can only remove an ALJ "for cause." 5 U.S.C. § 7521(a). Second, that determination of cause must be confirmed by the MSPB. MSPB members themselves can only be removed "for cause." *Id.*; 5 U.S.C. § 1202. Therefore, the judgment that an SEC ALJ should be removed for cause is "committed to another officer, who may or may not agree with the president's determination, and whom the President cannot remove simply because that officer disagrees with him." *Free Enter. Fund*, 561 U.S. at 484. Moreover, *Free Enterprise Fund* established that SEC commissioners themselves are only removable for

cause, *id.* at 487. Assuming that the Court was correct in *Free Enterprise Fund*, there exist in fact three layers of insulation between SEC ALJs and the president because commissioners themselves must initiate the removal proceedings against ALJs. 5 U.S.C. § 7521(a).

C. Even Officers in Quasi-Judicial Roles Like ALJs Must Be Removable by the President

Historical precedent going back to the Founding and this Court's direct on-point holdings show that even federal officials serving "quasi-judicial" roles like the ALJ position must be removable by the president.

The Court has held that even executive officers with a quasi-judicial role must not be beyond the president's power to remove any officer who fails to exercise the discretion required of the office intelligently or wisely. As it said in *Myers*:

> Then there may be duties of a quasi judicial character imposed on executive officers and members of executive tribunals whose decisions after hearing affect interests of individuals, the discharge of which the President cannot in a particular case properly influence or control. But even in such a case he may consider the decision after its rendition as a reason for removing the officer, on the ground that the discretion regularly entrusted to that officer by statute has not been on the whole intelligently or wisely exercised. Otherwise he does not discharge his own constitutional duty of seeing that the laws be faithfully executed.

272 U.S. at 135.

The president's power to remove quasi-judicial officers is not absolute like the power to remove purely executive officers; Congress can limit the removal of such quasi-judicial officers to "for-cause" reasons. *Humphrey's Executor v. United States*, 295 U.S. 602, 629 (1935). The removal for-cause still allows the president to see that the laws "be faithfully executed" but only so long as the president exercises direct authority to remove the officer for cause, or the power is exercised by an individual the president can remove without cause. *Free Enter. Fund*, 561 U.S. at 495-96.

History also shows that quasi-judicial executive officers must be subject to the presidential removal power. The first discussion of a quasi-judicial executive officer's removal occurred during the First Congress when considering the removal of the Comptroller of the Treasury. The Comptroller, due to his authority to decide claims between the United States and individual citizens, exercised power that was "not purely executive" but also included a "judicial quality." 1 Annals of Congress 635-36 (1789). Because of the quasi-judicial character of the office, Madison proposed that the tenure of the office be for "good behavior," but even so "the Comptroller would be dependent upon the President, because he can be removed by him." *Id.* Tenure based only on "good behavior" was necessary to "secure his impartiality," but even the need for impartiality was not sufficient to shield the officer entirely from the president's removal power. *Id.* This for-cause protection was too much for many of the other members of the First Congress and Madison eventually withdrew his motion. *Id.* at 637-39. The Court revived Madison's position in *Humphrey's Executor*, implementing his idea of limiting the removal of quasi-judicial executive

officers. Still, the president retained the power to remove the quasi-judicial officer for cause.

ALJs fulfill a more purely judicial function than either members of the Federal Trade Commission or the Comptroller of the Treasury. Their role may be more properly analogous to other non-Article III federal judges. While the president has never removed an Article III judge—the Constitution insulates them from such action—the president has removed many Article I judges without even giving cause and without congressional authorization. The power to remove these judges is essential to the president's ability to fulfill his duty. Before the Civil War, Attorney General John J. Crittenden was specifically asked about the presidential power to remove territorial judges, even without congressional authorization. He concluded:

> The President of the United States is not only invested with authority to remove the Chief Justice of the Territory of Minnesota from office, but it is his duty to do so if it appear that he is incompetent and unfit for the place. . . . Being civil officers, appointed by the President, by and with the advice and consent of the Senate, and commissioned by the President, they are not exempted from that executive power which, by the constitution, is vested in the President of the United States over all civil officers appointed by him.

5 U.S. Op. Atty. Gen. 288, 290 (1851). Crittenden opined that this removal power "has been long since settled, and . . . has ceased to be a subject of controversy or doubt." *Id.*

Then in *McAllister v. United States*, the Court interpreted the general statutory provisions for removal and replacement of "any civil officer . . . except judges of the courts of the United States" by the president as allowing the president to remove territorial judges. 141 U.S. 174 (1891). The quasi-judicial character of the office did not change the president's power to remove such executive officers.

When considering Congress's removal of the Comptroller General, the Court stated that "[i]nterpreting a law enacted by Congress to implement the legislative mandate" and "exercis[ing] judgment concerning facts that affect the application of the Act" are "[d]ecisions of that kind are typically made by officers charged with executing a statute." *Bowsher v. Synar*, 478 U.S. 714, 733 (1986).

The D.C. Circuit, in *Kuretski v. C.I.R.*, also considered the presidential removal of tax judges. In that case, the court held: "A tribunal may be considered a 'Court of Law' for purposes of the Appointments Clause notwithstanding that its officers may be removed by the President. The *Freytag* Court's treatment of territorial courts confirms the point." *Kuretski v. C.I.R.*, 755 F.3d 929, 941 (D.C. Cir. 2014), *cert. denied*, 135 S. Ct. 2309 (2015).

These examples include executive officers who exercise quasi-judicial functions as well as Article I judges that preside over a "court of law." ALJs sit somewhere in the middle of this continuum. That it is well-settled that the president must have the power to remove officers sitting at both ends of this spectrum, however, confirms that he must at least have the power to remove officers in the middle of it for cause.

* * *

In sum, ALJs are located squarely within the executive branch and remain executive officers who should be subject to control by superior officers (here the Commission) and ultimately the president. The Appointments Clause serves to control these officers at the front end, and the removal clause the back, as the Court has made clear in the series of cases that culminated in *Free Enterprise Fund*. The Court in that case simply set the question of ALJs aside, *Free Enter. Fund*, 561 U.S. at 507 n.10, but there is no constitutional basis to consider any type of executive officer in any way "immune" from the requirement of removability inherent in the separation of powers. If the Court were to recognize ALJs as a class of officers immune from removal by virtue of their quasi-judicial function, it would in effect be manufacturing a fourth branch of government.

CONCLUSION

Our Constitution requires that our government remain democratically accountable, so *amicus* asks the Court to reverse the D.C. Circuit and find that ALJs are officers of the United States and thus removable by the president.

Respectfully submitted,

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No. 17-130

In the Supreme Court of the United States

RAYMOND J. LUCIA
AND RAYMOND J. LUCIA COMPANIES, INC.,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICUS CURIAE* SUPPORTING PETITIONERS

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INTEREST OF THE *AMICUS CURIAE*

The Chamber of Commerce of the United States of America is the world's largest business federation. It represents 300,000 direct members and indirectly represents the interests of more than 3 million companies and professional organizations of every size, in every industry sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus curiae* briefs in cases that raise issues of concern to the Nation's business community.[1]

Businesses are frequently respondents in enforcement actions brought by the Securities and Exchange Commission (SEC). The Chamber accordingly has an interest in ensuring that the power to preside over those proceedings and to affect the interests of those businesses is vested in officials who are appointed in accordance with the requirements of the Constitution.

SUMMARY OF ARGUMENT

Administrative law judges (ALJs) presiding over enforcement actions brought by the SEC exercise very substantial authority.

Hundreds of companies and individuals have their rights and interests adjudicated in such pro-

[1] Pursuant to Rule 37.6, *amicus* affirms that no counsel for a party authored this brief in whole or in part and that no person other than *amicus*, its members, or its counsel made a monetary contribution to its preparation or submission. The parties' letters consenting to the filing of this brief have been filed with the Clerk's office.

ceedings each year. Recent statutory changes expanded the authority of these ALJs, authorizing them to preside over enforcement actions against virtually all companies and individuals and to impose remedies and penalties as broad as those available in an action in federal court.

Perhaps not coincidentally, the SEC has increased its use of administrative proceedings, where the Commission enjoys a higher rate of success and defendants are afforded fewer rights and protections than they are in federal courts.

These realities underscore the importance of ensuring that ALJs are appointed in a transparent and politically accountable manner. But they are not: Instead, they have been appointed through a complicated process involving numerous individuals who are several steps removed from elected officials—a process that not even the Commission's Division of Enforcement has been able to describe with confidence or accuracy.

This diffuse and opaque method of appointment is incompatible with the Appointments Clause. The Framers recognized that "the power of appointment to offices" was one of "the most insidious and powerful weapon of eighteenth century despotism." *Freytag* v. *Commissioner*, 501 U.S. 868, 883 (1991) (internal quotation omitted). The Framers sought to prevent abuse of the appointment power by limiting its dispersion and ensuring that "those who wielded it were accountable to political force and the will of the people." *Id.* at 884.

For that reason, all officers—*i.e.*, any official "exercising significant authority pursuant to the laws of the United States," *Buckley* v. *Valeo*, 424 U.S. 1, 126

(1976)—must be appointed by the President "with the Advice and Consent of the Senate," or, in the case of inferior officers, by "the President alone, in the Courts of Law, or in the Heads of Departments," as directed by Congress. U.S. Const. art. II, § 2, cl. 2.

This Court's precedents compel the conclusion that SEC ALJs are "officers" subject to the Appointments Clause. In *Freytag*, the Court held that special trial judges of the Tax Court qualify as "officers" based on characteristics and functions that are essentially indistinguishable from those of SEC ALJs—including "tak[ing] testimony, conduct[ing] trials, rul[ing] on the admissibility of evidence, and hav[ing] the power to enforce compliance with discovery orders." See 501 U.S. at 881-882. This exercise of "significant authority" renders both special trial judges of the Tax Court and SEC ALJs "officers" under the Appointments Clause.

In holding otherwise, the three-judge panel of the D.C. Circuit improperly dismissed this substantial collection of powers and the meaningful impact the Commission's increased use of SEC ALJs has on the business community, and elevated a single factor—SEC ALJs' purported lack of final decision-making authority—to dispositive status.

That analysis cannot be reconciled with the Court's decisions in *Freytag* and subsequent cases, which expressly rejected the argument that quasi-judicial officials must possess authority to enter final decisions to qualify as "officers" subject to the Appointments Clause. Nor can it be reconciled with the purpose of the Appointments Clause to "preserve political accountability relative to important government assignments." *Edmond* v. *United States*, 520 U.S. 651, 663 (1997).

This Court should reaffirm the Framers' limits on the appointment power and hold that SEC ALJs are inferior officers.

ARGUMENT

I. SEC ALJs Exercise Very Substantial Government Power.

Recent statutory changes have expanded the categories of persons who may be targeted through administrative actions and the remedies available to the SEC in such actions. These changes have enabled the Commission to bring many more enforcement actions in administrative proceedings before SEC ALJs, where the Commission has enjoyed a higher rate of success than it does in court.

That disparity, coupled with the reduced protections for respondents in administrative proceedings compared to enforcement actions in court, highlights the importance of ensuring compliance with constitutional requirements governing the appointment of the officials who preside over these administrative proceedings.

A. The Expanded Authority Of SEC ALJs

Recent statutory changes have expanded both the reach of SEC administrative proceedings and the range of available sanctions in those proceedings.

The Commission's ability to proceed through administrative proceedings was initially quite limited. These actions could be brought only against registered entities, and the only available relief was a "stop order" to halt an offering of securities to the public (see Securities Act of 1933, Pub. L. No. 73-22, § 8, 48 Stat. 74, 79-80) or rejecting an application for or revoking the registration of a broker-dealer or in-

vestment adviser (see Securities Exchange Act of 1934, Pub. L. 73-291, § 15, 48 Stat. 881, 895-896; Investment Company Act of 1940, Pub. L. 76-768, § 203, 54 Stat. 789, 850-852).

In the ensuing decades, the powers and jurisdiction of the SEC ALJs expanded, but until 2009, the authority to impose monetary penalties against persons or entities not registered with the Commission was for the most part limited to federal district courts. See, *e.g.*, Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. 101-429, §§ 102, 202-203, 301, 401, 104 Stat. 931, 933-935, 937-940, 941-945, 946-949. See also Andrew Ceresney, Dir., SEC Div. of Enft, Remarks to the American Bar Association's Business Law Section Fall Meeting (Nov. 21, 2014) (Ceresney Remarks), sec.gov/News/Speech/Detail/Speech/1370543515297 ("Until 2010, while we could proceed against unregistered persons in administrative proceedings, the relief that we could obtain against them was limited.").

In 2010, however, with the passage of the Dodd-Frank Act, the Commission gained the power to obtain through administrative proceedings virtually the same relief—including substantial monetary penalties—against the same broad set of individuals and entities that it could sue in federal district court. See *Ibid.* ("In the Dodd-Frank Act, * * * Congress provided us authority to obtain penalties in administrative proceedings against unregistered parties comparable to those we already could obtain from registered persons."); Jed S. Rakoff, *PLI Securities. Regulation Institute Keynote Address: Is the S.E.C. Becoming a Law Unto Itself?* 5 (Nov. 5, 2014) (Rakoff), perma.cc/4JBL-KRPW ("The net result of all this is that the S.E.C. can today obtain through

internal administrative proceedings nearly everything it might obtain by going to court."); Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, § 929P, 124 Stat. 1376, 1862-1865.

Now the Commission can proceed administratively against *any* person or entity. See 15 U.S.C. 77h-1, 78u-3(a), 80a-9(f), 80b-3(k). And it can obtain in those proceedings monetary and other civil penalties such as fines (including against unregistered persons) (see *id.* §§ 77h-1(e) and (g), 78u-2, 78u-3(e), 80a-9(d) and (e), 80b-3(i) and (k)); cease and desist orders (see *id.* §§ 77h-1, 78u-3(a), 80a-9(f), 80b-3(k)); and collateral bars prohibiting individuals from associating with entities regulated by the SEC (see *id.* §§ 78o(b)(6)(A), 78o-4(c)(4), 78q-1(c)(4)(C), 80b-3(f)).

B. The Commission's Increased Use of Its In-House Administrative Proceedings

The expansion of SEC ALJs' authority paved the way for a dramatic shift in the SEC's use of administrative proceedings.

The Director of the Commission's Division of Enforcement, Mr. Ceresney, announced in 2013 that the SEC intended to funnel enforcement actions into administrative proceedings before SEC ALJs as opposed to federal court: "Our expectation is that we will be bringing more administrative proceedings given the recent statutory changes." Gretchen Morgenson, *At the S.E.C., a Question of Home-Court Edge*, N.Y. Times, Oct. 5, 2013, goo.gl/eJfeoG.

A year later, Mr. Ceresney confirmed that "[t]here is no question that we are using the administrative forum more often now than in past years, giv-

en the changes under Dodd-Frank." Ceresney Remarks, *supra*, page 5; see also Jean Eaglesham, *SEC Is Steering More Trials to Judges It Appoints*, Wall Street J., Oct. 21, 2014, goo.gl/WwLm7H (quoting head of SEC's anti-foreign-corruption enforcement unit as saying that "[i]t's fair to say it's the new normal" to use administrative judges).

The data confirms that statement. In 2014, the Commission instituted 610 administrative proceedings—more than double the number instituted in 2005. Ryan Jones, *The Fight Over Home Court: An Analysis of the SEC's Increased Use of Administrative Proceedings*, 68 SMU L. Rev. 507, 509 (2015). See also SEC, *Select SEC and Market Data: Fiscal 2014* 3, sec.gov/files/secstats2014.pdf. Indeed, the increased use of administrative proceedings was so dramatic that, in late 2014, the Commission almost doubled the number of SEC ALJs by adding two new ALJs. See SEC, *Press Release: SEC Announces New Hires in the Office of Administrative Law Judges* (June 30, 2014), perma.cc/TZ5U-HBJ6; Yaron Nili, *SEC Enforcement Developments in 2014, and a Look Forward*, Harv. L. Sch. F. on Corp. Governance & Fin. Reg. (Mar. 18, 2015), perma.cc/A9QL-LWBW.

C. The Commission's Increased Use Of Administrative Proceedings Adversely Affects Companies And Individuals.

The Commission's decision to utilize administrative enforcement proceedings rather than actions in federal court was not a neutral forum change. Significant differences between the proceedings impact the rights and interests of companies and individuals subject to the SEC's regulations and enforcement authority. The decision to focus on administrative proceedings has raised serious questions of fairness for

those businesses and individuals. See U.S. Chamber of Commerce, *Examining U.S. Securities and Exchange Commission Enforcement: Recommendations on Current Processes and Practices* (July 2015) (U.S. Chamber SEC Enforcement Report).

First, the Commission enjoys a higher rate of success in its proceedings before SEC ALJs than in civil court actions. Between October 2010 and March 2015, the SEC won 90% of the cases it brought before its ALJs, as compared with 69% of cases before district court judges. Jean Eaglesham, *SEC Wins With In-House Judges*, Wall Street J., May 6, 2015, goo.gl/N5FgXV.

The Commission won *every one* of the 219 administrative decisions issued between October 2013 and January 2015. Jones, 68 SMU L. Rev. at 509.

Many commentators, including one Commissioner, have asserted that this "home court" advantage is the reason why the Commission shifted enforcement cases into administrative proceedings: "[T]his change has the appearance of the Commission looking to improve its chances of success by moving cases to its in-house administrative system." Michael S. Piwowar, Comm'r, SEC, Remarks at the "SEC Speaks" Conference 2015: A Fair, Orderly, and Efficient SEC (Feb. 20, 2015), sec.gov/news/speech/022015-spchcmsp.html#_ftnref3.

Indeed, for several years after Dodd-Frank's enactment, the Commission rarely brought insider trading cases in administrative proceedings. Following a string of high-profile insider trading losses, however, the SEC announced its intention to start bringing more insider trading cases in administrative proceedings. See Ronald E. Wood, *SEC May*

Ramp Up Administrative Proceedings, Daily Journal Supplement, July 23, 2014, at 7, goo.gl/xpyuNT; Brian Mahoney, *SEC Could Bring More Insider Trading Cases In-House*, Law360 (June 11, 2014), perma.cc/5QNS-79VP. And it did. See SEC, *Select SEC and Market Data: Fiscal 2016* 3, sec.gov/files/2017-03/secstats2016.pdf; Jean Eaglesham, *SEC Is Steering More Trials to Judges It Appoints*, Wall Street J., Oct. 21, 2014, goo.gl/WwLm7H.

Second, the procedural rules applicable in administrative proceedings before ALJs differ from federal court cases in several ways that meaningfully impact the ability of charged parties to present a full defense.

For example, pre-hearing discovery is limited, respondents have a shorter period of time to prepare for a hearing, the evidentiary safeguards of the Federal Rules of Evidence do not apply, and there is no right to a jury trial. See U.S. Chamber SEC Enforcement Report at 11-21; Joseph A. Grundfest, *Fair or Foul?: SEC Administrative Proceedings and Prospects for Reform Through Removal Legislation*, 85 Fordham L. Rev. 1143, 1156-1165, 1169-1174 (2016) (Grundfest); Stephen J. Choi & A.C. Pritchard, *The SEC's Shift to Administrative Proceedings: An Empirical Assessment*, 34 Yale J. on Reg. 1, 13-14 (2017) (Choi & Pritchard).

The lack of discovery and shorter trial preparation time is particularly harmful, because the SEC staff—by contrast—may take years to investigate and develop a case, during which time it has essentially unfettered authority to request documents and interview witnesses. See Grundfest at 1158. The imbalance between the SEC and defendants in admin-

istrative proceedings has raised concerns about the fairness of such proceedings.

The disadvantages of administrative proceedings to defendants are so substantial that even the threat of bringing an administrative proceeding has provided the Commission with significant leverage in inducing defendants to cooperate or settle. See Choi & Pritchard at 21-22. As former SEC Enforcement Director Ceresney acknowledged, "There have been a number of cases in recent months where we had threatened administrative proceeding . . . and they settled." Sarah N. Lynch, *U.S. SEC to File Some Insider-Trading Cases in Its In-House Court*, Reuters, June 11, 2014, perma.cc/X9UJ-MZ4M.

Moreover, the real-world impact of decisions by SEC ALJs extends beyond the individual enforcement actions over which the ALJs preside. Agencies, and particularly the SEC, have long used administrative proceedings to establish generally applicable standards and policies—eschewing the formal rulemaking process in favor of case-by-case adjudication. See David L. Shapiro, *The Choice of Rulemaking or Adjudication in the Development of Administrative Policy*, 78 Harv. L. Rev. 921, 926 (1965); *SEC* v. *Chenery Corp.*, 332 U.S. 194, 201-203 (1947).

The increased use of administrative proceedings accordingly produces a correspondingly greater role for ALJs in agency policymaking. It also transfers responsibility for construing and interpreting the securities laws from federal courts to ALJs because federal courts reviewing administrative decisions defer to ALJs' legal conclusions. See Rakoff at 10-12; Grundfest at 1149, 1166-1167.

Indeed, the SEC's own internal guidance on forum selection recommends bringing an enforcement action as an administrative proceeding before an in-house ALJ, as opposed to as a civil action in court, if it "is likely to raise unsettled and complex legal issues under the federal securities laws, or interpretation of the Commission's rules." SEC, *Division of Enforcement Approach to Forum Selection in Contested Actions* 3, goo.gl/3nXWwC.

II. SEC ALJs Have Been Hired Using A Diffuse And Opaque Process.

The important responsibilities exercised by SEC ALJs in enforcement proceedings should require a selection process that clearly locates the responsibility for appointing these officials.

But SEC ALJs are appointed through a convoluted process involving low-ranking federal employees. Indeed, the process by which SEC ALJs are hired is so impenetrable that even the Commission itself has had difficulty determining by whom and through what process SEC ALJs are appointed.[2]

In *Matter of Timbervest*, the Division of Enforcement submitted an affidavit purporting to "set[] forth the manner in which administrative law judge ('ALJ') Cameron Elliot and Chief ALJ Brenda Murray were hired, including the method of selection and appointment." Notice of Filing at 1, *Timbervest, LLC*, SEC Admin. Proceeding File No. 3-15519 (June 4, 2015), sec.gov/litigation/apdocuments/3-15519-event-

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[2] In November 2017, after filing its response to the certiorari petition in this case, the SEC purported to ratify the prior appointment of the current SEC ALJs. SEC, *Pending Administrative Proceedings*, sec.gov/litigation/opinions/2017/33-10440.pdf.

139.pdf. The Division explained that under the then-applicable statutes and regulations, the SEC hired its ALJ through a process overseen by the U.S. Office of Personnel Management (OPM). *Id.* at 2.

OPM administers the competitive examination for selecting ALJs and provides to the SEC Chief ALJ a list of eligible candidates. *Ibid.* The Chief ALJ and an interview committee then make a preliminary selection from the top three candidates on the list, which is subject to final approval and processing by the SEC's Office of Human Resources. *Ibid.*

However, the Division admitted that it could not state with certainty how and by whom Chief ALJ Murray was appointed because "it is possible that internal [hiring] processes have shifted over time," and "information regarding hiring practices at [the time Chief ALJ Murray was hired] is not readily accessible." *Id.* at 2-3.

Furthermore, although the Division asserted that ALJ Elliot was hired pursuant to the procedures set forth in the affidavit, it explained in a subsequent filing that its description of how ALJ Elliot was hired was incorrect. As ALJ Elliot himself stated at a hearing in another case, "the Division's description of how I was hired [in the *Timbervest* affidavit] was erroneous." Br. of Respondents to the Commission's May 27, 2015 Order, *Timbervest, LLC*, SEC Admin. Proceeding File No. 3-15519 (June 23, 2015), Exhibit C (June 18 and June 19, 2015 Hearing Transcripts, *Bebo and Buono*, SEC Admin. Proceeding File No. 3-16293 (June 18, 2015)). Because he had been an ALJ in the Social Security Administration prior to being hired as an SEC ALJ, he simply sent in his resume in response to a posting on the federal government's job-posting website, interviewed, and was given an

offer. Notably, he still could not say who appointed him.

This window into the appointment process illustrates that those who appoint SEC ALJs are far removed from any accountability for the consequential actions of the SEC ALJs they appoint: Not only are those individuals unelected, and also not appointed by the President and confirmed by the Senate, but they are also largely indiscernible to the public. This diffusion of responsibility is the precise evil that the Framers sought to prevent by including the Appointments Clause in the Constitution.

III. SEC ALJs Are "Officers" Who Must Be Appointed In Accordance With The Appointments Clause.

A. The Clause Ensures Accountability For Appointments Of Officials Who Exercise Significant Executive Authority.

The Constitution's separation of powers, with its attendant checks and balances, is "essential to the preservation of liberty," and also ensures that "[a] dependence on the people" is the "primary control on the government." The Federalist No. 51, at 261-262 (James Madison) (Garry Wills ed., 1982). The Appointments Clause is "among the significant structural safeguards of the constitutional scheme." *Edmond* v. *United States*, 520 U.S. 651, 659 (1997); see also *Freytag* v. *Commissioner*, 501 U.S. 868, 880 (1991). It serves this role in two ways.

First, the Clause "prevents congressional encroachment upon the Executive and Judicial Branches" by "vesting the President with the exclusive power to select the principal (noninferior) officers of the United States." *Edmond*, 520 U.S. at 659.

Second, with respect to "inferior Officers," the Clause grants Congress "only limited authority to devolve appointment power on the President, his heads of departments, and the courts of law." *Freytag*, 501 U.S. at 884. See also U.S. Const. art. II, § 2, cl. 2; *Weiss* v. *United States*, 510 U.S. 163, 184-185 (1994); *Ryder* v. *United States*, 515 U.S. 177, 182 (1995) ("The [Appointments] Clause is a bulwark against one branch aggrandizing its power at the expense of another branch.").

Third, by limiting the power of appointment to the President and, in the case of inferior officers, to the heads of departments and the courts, the Appointments Clause ensures that those wielding the appointment power are "accountable to political force and the will of the people." *Freytag*, 501 U.S. at 878, 884. The Framers recognized that when the power of appointment is dispersed among multiple people, "[s]candalous appointments to important offices" are made, and it is impossible to "determine[] by whose influence [the people's] interests have been committed to hands so unqualified, and so manifestly improper." The Federalist No. 70 at 359 (Alexander Hamilton) (Garry Wills ed., 1982). Accordingly, the Constitution "carefully husband[s] the appointment power to limit its diffusion" (*Freytag*, 501 U.S. at 883) and thus permits the people to "determine what part had been performed by the different actors" (The Federalist No. 77 at 389 (Alexander Hamilton) (Garry Wills ed., 1982)). That in turn ensures that those wielding the appointment power are "accountable to political force and the will of the people." *Freytag*, 501 U.S. at 884.

Consistent with this history, the Court has held that "any appointee exercising significant authority

pursuant to the laws of the United States" is an "Officer of the United States" who must be appointed in accordance with the Appointments Clause. *Buckley* v. *Valeo* 424 U.S. 1, 126 (1976); see also *id.* at 132 ("Unless their selection is elsewhere provided for, *all* Officers of the United States are to be appointed in accordance with the Clause." (emphasis added)); *Freytag*, 501 U.S. at 881.

The class of officials covered by the Clause is "unusually broad," including:

> (1) A district court clerk, [*Ex parte Hennen*, 38 U.S. 230, 257-258 (1839)]; (2) "thousands of clerks in the Departments of the Treasury, Interior and the othe[r]" departments, [*United States* v. *Germaine*, 99 U.S. 508, 511 (1878)], who are responsible for "the records, books, and papers appertaining to the office," [*Hennen*, 38 U.S. at 259]; (3) a clerk to "the assistant treasurer" stationed "at Boston," [*United States* v. *Hartwell*, 73 U.S. 385, 392 (1868)]; (4 & 5) an "assistant-surgeon" and a "cadet-engineer" appointed by the Secretary of the Navy, [*United States* v. *Moore*, 95 U.S. 760, 762 (1878); *United States* v. *Perkins*, 116 U.S. 483, 483 (1886)]; (6) election monitors, [*Ex parte Siebold*, 100 U.S. 371, 397-399 (1880)]; (7) United States attorneys, [*Myers* v. *United States*, 272 U.S. 52, 159 (1926)]; (8) federal marshals, [*Siebold*, 100 U.S. at 397; *Morrison* v. *Olson*, 487 U.S. 654, 676 (1988)]; (9) military judges, [*Weiss*, 510 U.S. at 170]; (10) judges in Article I courts, [*Freytag*, 501 U.S. at 892]; and (11) the general counsel for the Department of Transportation, [*Edmond*, 520 U.S. at 666].

Free Enter. Fund v. *Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 539-540 (2010) (Breyer, J., dissenting) (citations altered).

Particularly relevant to determining the status of SEC ALJs is this Court's holding in *Freytag* that special trial judges of the U.S. Tax Court are "inferior officers" based on the "significance of the duties and discretion that [they] possess." 501 U.S. at 881. The Court emphasized that special trial judges "perform more than ministerial tasks"; they "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders," and they exercise significant discretion in carrying out those "important functions." *Id* at 881-882.[3]

Since *Freytag*, this Court held—virtually summarily—that military judges are officers subject to the Appointments Clause. See *Edmond*, 520 U.S. at 662; *Weiss*, 510 U.S. at 169-170.

B. SEC ALJs Are "Officers" Because They Exercise Significant Authority Pursuant To The Laws Of The United States.

The Court's precedents make clear that SEC ALJs are "Officers" required to be appointed in compliance with the Appointments Clause.

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[3] The Court held in the alternative that "[e]ven if the duties of special trial judges" in cases in which they did not have final decision-making authority "were not as significant as [it had] found them to be," the judges' authority to enter final decisions in other cases would suffice to make them "officers." *Id.* at 882.

1. SEC ALJs exercise significant authority.

The authority and discretion of SEC ALJs are indistinguishable from the duties of the special trial judges that the *Freytag* Court found sufficiently "significan[t]" to render special trial judges "officers" under the Appointments Clause. 501 U.S. at 881-882.

The SEC has delegated to ALJs responsibility for the "fair and orderly conduct of [administrative] proceedings" (17 C.F.R. 200.14(a)), and thereby empowered the ALJs to "perform more than ministerial tasks" (*Freytag*, 501 U.S. at 881).[4] An SEC ALJ has "authority to do all things necessary and appropriate to discharge his or her duties." 17 C.F.R. 201.111. That includes, but is not limited to: issuing, revoking, quashing, and modifying subpoenas; receiving evidence and ruling on the admissibility of evidence and offers of proof; regulating the course of a proceeding and the conduct of the parties and their counsel; examining witnesses; ordering and regulating document production and depositions; ruling on all procedural and other motions; sanctioning contemptuous conduct; and preparing an initial decision containing factual findings and legal conclusions, the reasons or basis thereof, and an appropriate order, sanction, and relief. *Id.* §§ 200.14(a), 201.111,

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[4] Like the office of special trial judge, the office of SEC ALJ is established by law. The Administrative Procedure Act creates the office of the administrative law judge, and sets forth the ALJ's duty of presiding over adjudicatory hearings. 5 U.S.C. 556, 557; see also *id.* §§ 3105, 5372 (setting forth means of appointment and salary). The federal securities laws, in turn, authorize the SEC to "delegate * * * any of its functions to * * * an administrative law judge." 15 U.S.C. 78d-1(a).

201.180, 201.230, 201.233, 201.360. See also 5 U.S.C. 557(c). See generally 5 U.S.C. 556(c).

The ALJ's initial decision is "deemed the action of the [SEC]," unless a party or other person entitled to review files a timely petition for review or the SEC on its own initiative exercises its discretionary right to review. 15 U.S.C. 78d-1(c). See also 17 C.F.R. 201.360(d); 5 U.S.C. 557(b). Even in those cases in which a party appeals the ALJ's decision, the SEC retains discretion to decline to review the ALJ's decision, except in a few specified circumstances. See 17 C.F.R. 201.411(b). As a practical matter, 90 percent of ALJ initial decisions become final without review by the SEC. See *Bandimere* v. *United States*, 844 F.3d 1168, 1187 (10th Cir. 2016).

In other words, SEC ALJs "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders." *Freytag*, 501 U.S. at 881-882.[5] And "[i]n the course of carrying out these important functions, the [ALJs] exercise significant discretion." *Id.* at 882. These characteristics, which led the Court in *Freytag* to find special trial judges of the Tax Court to be "Officers" subject to the Appointments Clause, likewise compel the conclusion that SEC ALJs are "Officers."

2. Final decision-making authority is not an indispensable characteristic of "Officers."

The D.C. Circuit panel rested its contrary conclusion solely on the fact that SEC ALJs lack the au-

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[5] Although SEC ALJs do not have the power to impose fines or imprisonment for contempt, they have the authority to impose other sanctions for contemptuous conduct. See 17 C.F.R. 201.180.

thority to issue final decisions. Pet. App. 13 ("Our analysis begins, and ends," with the question of "whether Commission ALJs issue final decisions of the Commission."). That determination, however is inconsistent with this Court's decision in *Freytag*, and with the Court's subsequent decisions interpreting the Appointments Clause.

The *Freytag* Court squarely *rejected* the argument that "special trial judges may be deemed employees in [certain cases] because they lack authority to enter a final decision." 501 U.S. at 881. That view, the Court held, "ignore[d] the significance of the duties and discretion that special trial judges possess" (*ibid.*)—statutorily established office, duties, salary, and means of appointment, and performance of the "important functions" of "tak[ing] testimony, conduct[ing] trials, rul[ing] on the admissibility of evidence, and hav[ing] the power to enforce compliance with discovery orders." *Id.* at 881-882.

It was on the basis of these "significan[t]" duties and the "significant discretion" special trial judges had in performing those duties—the very same powers possessed by SEC ALJs—that the Court held that special trial judges were officers for purposes of the Appointments Clause. *Ibid.*

To be sure, after the Court found that special trial judges qualified as "officers" based on their role and discretion in regulating the trial process, it went on to set forth a separate and independent basis for finding the judges to be officers. "*Even if* the duties of special trial judges" were not as significant as the Court had just found them to be—and thus not sufficient by themselves to qualify special trial judges as officers—the Court's conclusion that special trial judges are inferior officers "would be unchanged" be-

cause special trial judges have the authority to enter final decision in some categories of cases. *Id.* at 882 (emphasis added).

That authority, the Court explained, was sufficient to categorize special trial judges as inferior officers in all cases, even if the Court assumed that in some cases the judges had neither final decision-making authority nor other significant duties. *Id.* In other words, *Freytag* stands for the proposition that final decision-making authority in some matters would be sufficient to make an official an "officer" for all purposes, even where his other functions are not "significant." But final decision-making authority in all matters is not necessary for "officer" designation.

Subsequent cases confirm this interpretation of *Freytag*. In *Weiss*, decided just a few years after *Freytag*, this Court held that military judges qualify as officers subject to the requirements of the Appointments Clause. See 510 U.S. at 170. Military judges "rule[] on all legal questions, and instruct[] court-martial members regarding the law and procedures to be followed," and, where the accused elects, decide guilt or innocence and impose sentences. *Id.* at 167-168.

However, "[n]o sentence becomes final until it is approved by the officer who convened the court-martial," and the judges' factual findings, legal rulings, and sentences are subject to *de novo* review by the Courts of Military Review.[6] *Id.* at 168. See also *id.* at 193 (Souter, J., concurring); 10 U.S.C. 864, 866,

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[6] The Courts of Military Review were renamed the Courts of Criminal Appeals. See National Defense Authorization Act for Fiscal Year 1995, Pub. L. 103-337, § 924, 108 Stat. 2663, 2831 (1994).

869. Notwithstanding the military judges' inability to enter final decisions, the Court held that "because of the authority and responsibilities they possess," military judges "act as 'Officers' of the United States." *Weiss*, 510 U.S. at 169.[7]

Similarly, in *Edmond*, the Court held that judges on the Coast Guard Court of Criminal Appeals are inferior officers for purposes of the Appointments Clause. 520 U.S. at 666. The Court expressly recognized that those judges "have no power to render a final decision on behalf of the United States unless permitted to do so by other executive officers." *Id.* at 665. Nevertheless, the Court "[did] not dispute that military appellate judges are charged with exercising significant authority on behalf of the United States," which rendered them officers under the Appointments Clause. *Id.* at 662.

Indeed, the Court recognized that being subject to review is inherent to the definition of an "inferior officer," who is subject to the Appointments Clause: "[W]e think it evident that 'inferior officers' are officers whose work is directed and supervised at some level by others who were appointed by presidential nomination with the advice and consent of the Senate." *Id.* at 663.

Thus, in both *Weiss* and *Edmond*, this Court confirmed that the authority to enter final decisions is relevant to distinguishing *inferior* officers from *principal* officers, not to distinguish inferior officers from

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[7] The precise issue in *Weiss* was whether the Appointments Clause requires military officers to obtain a separate appointment before serving as military judges. The Court noted that the parties agreed "rightly so" that the Appointments Clause applied to the military judges. 510 U.S. at 170.

mere employees whose appointments are not subject to the strictures of the Appointments Clause. The decision below cannot be squared with these precedents, and the interpretation of the Clause that it embraced unjustifiably excludes scores of officials with significant influence over the interests of the people from the accountability-preserving protections of the Appointments Clause.

* * *

The Appointments Clause is no mere formality; and its application similarly does not turn on a formalistic rule based solely on whether an official possesses final decision-making authority. Rather, the Framers recognized that officers—both inferior and principal—exercise government authority that can profoundly influence the lives and interests of the people. They therefore sought to "preserve political accountability relative to important government assignments" by enshrining in the Constitution a carefully cabined and transparent method of appointing individuals to such assignments. *Edmond*, 520 U.S. at 662.

The SEC ALJs at issue here unquestionably hold "important government assignments," and therefore must be appointed pursuant to the requirements of the Appointments Clause so that the people may hold the appointing authority—and ultimately the President—accountable for the consequential actions of SEC ALJs.

By some estimates, there are approximately 1,500 other ALJs across all federal agencies, see *Free Enter. Fund*, 561 U.S. at 542-543 (Breyer, J., dissenting); *Bandimere*, 844 F.3d at 1199 (McKay, J., dissenting), of which fewer than 200 preside over adver-

sarial proceedings as SEC ALJs do. But whether those other ALJs are also officers for purposes of the Appointments Clause turns on the scope of their particular functions and duties. And whether there is a violation of the Appointments Clause turns on how those ALJs are selected.[8]

Importantly, holding that an official was appointed in violation of the Appointments Clause does not automatically invalidate all of that official's decisions. Applying the *de facto* officer doctrine, the Court has precluded collateral Appointment Clause challenges to decisions that have become final—considering such challenges when, as here, the issue is raised on direct review. See, *e.g.*, *Ryder* v. *United States*, 515 U.S. 177 (1995).

CONCLUSION

The judgment of the court of appeals should be reversed.

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[8] In addition, the number of ALJs is dwarfed by the "*thousands* of clerks in the Departments of the Treasury, Interior and the othe[r]" departments who the Court has recognized are officers for purposes of the Appointments Clause. *Germaine*, 99 U.S. at 511 (emphasis added).

Respectfully submitted.

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No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, *et al.*,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DC CIRCUIT

BRIEF FOR WING F. CHAU AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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INTEREST OF THE *AMICUS CURIAE*[1]

In the wake of the financial crisis that began in 2007, the U.S. Securities and Exchange Commission (the "Commission" or SEC) investigated finance professionals and firms that participated in various ways in the creation and marketing of securities such as Collateralized Debt Obligations (CDOs) whose demise was blamed for precipitating the crisis. *Amicus curiae* Wing F. Chau is a principal of Harding Advisory, LLC, a collateral manager who analyzed and helped select collateral securities for a number of CDOs (and managed those CDOs) until they experienced events of default when the crisis hit. In October 2013, the SEC charged Mr. Chau and Harding Advisory (collectively, "Harding") with fraud in connection with the assembly of collateral for and marketing of one CDO and also in connection with purchasing certain bonds of a non-Harding CDO for two other CDOs that Harding managed. These charges were brought administratively, and the hearing was assigned to SEC Administrative Law Judge (ALJ) Cameron Elliot, the same ALJ who presided over the Petitioners' case. Harding is one of the petitioners to the U.S. Court of Appeals for the District of Columbia Circuit whose petition is being held in abeyance pending the resolution of this case. Brief for Petitioners at 48-49, *Lucia v. SEC*, No. 17-130 (Feb. 21, 2018) ("Pet'rs Br.").

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1. Pursuant to this Court's Rule 37.6, counsel for *amicus curiae* certifies that this brief was not authored in whole or in part by counsel for any party and that no person or entity other than *amicus curiae* or his counsel made a monetary contribution intended to fund the preparation or submission of this brief. Both Petitioners and Respondent have consented to the filing of this brief.

Despite the fact that, as demonstrated in this brief, Congress intended SEC administrative hearings to be conducted by officers of the United States because of the power they wield and to assure fairness, competence, and political accountability, numerous crucial decisions that drove the outcome of Harding's case were made by ALJ Elliot (who was not properly appointed) or by other SEC employees who acted on behalf of the Commission and exercised its power also without proper appointment. In other words, not a single properly-appointed officer can be held accountable for these decisions; neither the Commission, nor any individual Commissioner, and not ALJ Elliot. As a result, the Commission can disclaim political accountability by pretending that an "independent" ALJ made the relevant decisions and ALJ Elliot can disclaim responsibility by relying on SEC processes and procedures. The Commission should not be allowed to treat constitutional and congressional prescriptions about delegation of authority and diffusion of political responsibility so lightly.

Treating constitutional edicts as suggestions not commands, both the Commission and ALJ Elliot cloaked ALJ Elliot in the trappings of an officer without appointing him as one. The SEC described ALJ Elliot's functions as those of an officer:

> Administrative law judges are independent judicial officers who rule on allegations of securities law violations in public administrative proceedings instituted by the Commission. They conduct public hearings, in a manner similar to non-jury trials in federal district courts, issue

> initial decisions, and have authority to impose a broad range of sanctions.

Press Release, SEC Announces Arrival of New Administrative Law Judge Cameron Elliot, U.S. Sec. & Exch. Comm'n (Apr. 25, 2011), https://www.sec.gov/news/press/2011/2011-96.htm. To command respect and exude authority, ALJ Elliot signed subpoenas as "an officer designated by the Securities and Exchange Commission," allowed himself to be called "Your Honor," and had litigants stand up when he entered the courtroom or when they addressed him.[2] *See* Subpoena *Ad Testificandum*, *In re Harding Advisory LLC*, Admin. Proc. File No. 3-15574 (Mar. 14, 2014), attached as Exhibit, at 1a.

It is no accident, therefore, that the case against Harding was brought administratively; with no one responsible, no one needed to take responsibility for any unfairness, and the proceeding was rife with unfairness. The starkest example of this is the management of the hearing schedule. The issues in Harding's case were highly complex and involved a very large volume of material. (The Division of Enforcement's initial production alone was the equivalent of the entire printed contents of the Library of Congress.) Because of the complexity and the volume of materials, Harding asked ALJ Elliot for an additional six months to prepare for the hearing. (At the time, SEC Rules of Practice required the issuance of the initial decision of the ALJ within 300 days of service of the order instituting proceedings.) *See* Supplemental

2. His representation that he was "an officer of the Commission" is, of course, a misrepresentation. He is an employee who performed officer functions without proper appointment.

Briefing in Support of Respondents' Appeal Regarding Their Due Process Claims at 4-5, *In re Harding Advisory, LLC*, Admin. Proc. File No. 3-15574 (June 9, 2015).[3]

In response to Harding's motion to extend the 300-day deadline by six months, ALJ Elliot claimed that he sympathized but that his hands were tied by the Commission, and then denied the request. *See* Order Denying Respondent's Motion for Adjournment at 1-2, *In re Harding Advisory, LLC*, Admin. Proc. File No. 3-15574, 2014 WL 10937716, at *1-2 (Jan. 24, 2014). When Harding filed an interlocutory appeal of this denial to the Commission, the Commission itself did not rule. Rather, the SEC's Office of General Counsel ruled on the appeal **by delegated authority**; none of the Commissioners was involved in that decision. *See* Order Denying Petition for Interlocutory Review and Emergency Motion to Stay the Hearing and Prehearing Deadlines at 14, *In re Harding Advisory, LLC*, Admin. Proc. File No. 3-15574, 2014 WL 988532, at *8 (Mar. 14, 2014). In other words, not a single properly-appointed officer of the United States ruled on something as significant as whether the arbitrary deadline imposed by the Commission Rules of Practice deprived Harding of the ability to prepare adequately. Ironically, despite denying Harding six additional months to prepare—and finding that "one day" there may be "an administrative proceeding where the difficulties of preparing for hearing [sic] within the time specified . . . are found to warrant some extraordinary relief . . . but this is not that proceeding," *see id.* at 2—after the hearing, ALJ Elliot asked the Commission for four additional

3. The SEC docket for *In re Harding Advisory, LLC*, Admin. Proc. File No. 3-15574, can be located at: https://www.sec.gov/litigation/apdocuments/ap-3-15574.xml.

months to file his initial decision, citing the volume of the record and the complexity of the issues. The Commission granted his request. *See* Order Granting Extension, *In re Harding Advisory, LLC*, Admin. Proc. File No. 3-15574, 2014 WL 4160053 (Aug. 21, 2014) (noting, among other things, that ALJ Elliot "held seventeen days of hearing [sic] in this matter, which involved nearly 5,000 pages of transcript, nearly 1,400 exhibits, and more than 500 pages of post-hearing briefs," and finding that it was in the public interest to extend the deadline).

Another indication of the SEC and ALJ Elliot taking officer status lightly is ALJ Elliot's apparent view that if the Commission alleged liability, it was his job to find liability. As the Petitioners note, ALJ Elliot invariably found for the Commission in his first three years as an ALJ—50 out of 50 cases. *See* Pet'rs Br. at 6; Jean Eaglesham, *Fairness of SEC Judges Is in Spotlight*, Wall St. J. (Nov. 22, 2015), https://www.wsj.com/articles/fairness-of-sec-judges-is-in-spotlight-1448236970 (stating that as of November 22, 2015, ALJ Elliot "has found the defendants liable in every contested case he has heard" and that "[h]e dismissed a case for the first time in August").[4]

4. It appears that in the one referenced instance of ALJ Elliot ruling for the respondent, he also found liability but refused to impose sanctions based on the respondent's personal circumstances. *See In re Judy K. Wolf*, Admin. Proc. File No. 3-16195, 2015 WL 4639230, *19-23 (Aug. 5, 2015). Since November 22, 2015, ALJ Elliot has issued 59 initial decisions, and all but two of these decisions have been adverse for the respondents. However, neither outcome in those cases alters ALJ Elliot's record. *See In re GCA Acquisition Corp.*, Admin. Proc. File No. 3-17868, 2017 WL 2000697, at *1 (May 12, 2017) ("After investigating the matter, the Division filed a brief and a declaration expressing the belief that the proceeding against

Indeed, in Harding's case, ALJ Elliot was so determined to find liability that he adopted an uncharged negligence theory when it became clear that there was no evidence to support the Commission's allegation of willfulness, stating: "in order to find an intent to defraud, I would have to disbelieve every single lay witness who testified on the subject." Initial Decision at 66, *In re Harding Advisory, LLC*, Admin. Proc. File No. 3-15574, 2015 WL 137642, at *63 (Jan. 12, 2015). Despite ALJ Elliot's effort to do the Commission's bidding, even the Commission recognized that the uncharged negligence theory was defective and reversed. Opinion of the Commission at 6-7, *In re Harding Advisory, LLC*, Admin. Proc. File No. 3-15574, 2017 WL 66592, at *5 (Jan. 6, 2017). ALJ Elliot's second finding of liability (with respect to the purchase of two non-Harding bonds for two Harding-managed CDOs—each of these bonds represented approximately 1.6% of the collateral of each of those Harding-managed CDOs) is similar. Here, ALJ Elliot found that Harding bought the two bonds despite having a negative opinion of them. Not a single witness testified that Harding disliked the bonds. Mr. Chau denied disliking the bonds. But ALJ Elliot did not find Mr. Chau credible and the Commission later upheld ALJ Elliot's finding of liability, in large part, by deferring to ALJ Elliot's credibility findings. *See id.* at 15-17, 2017 WL 66592, at *12-13. It is worth pointing out, however, that ALJ Elliot's credibility findings on issues of asset selection may have been infected by his failure to understand the instruments at issue; despite contrary

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International Metals should be dismissed."); *In re Gary L. McDuff*, Admin. Proc. File No. 3-15764, 2016 WL 7324412, at *2, 17-18, 20 (Dec. 16, 2016) (ALJ Elliot dismissed claims after the Commission reversed his prior finding of liability on the pleadings in a case involving a *pro se* defendant serving 300 months in prison).

testimony and disclosures in the relevant deal documents, he did not understand that the securities Harding selected for its CDOs were investment grade. Initial Decision at 4, *In re Harding Advisory, LLC*, 2015 WL 137642, at *4.

Mr. Chau submits this brief to demonstrate that Congress understood that the power wielded by SEC ALJs is immense and the consequences of their actions are grave, and thus that the constitutional requirements for officers and their appointment are meaningful. The SEC's shifting claims that ALJs are akin to U.S. district court judges conducting trials, but that they are mere employees, and most recently, that their initial defective appointments can be "ratified," make a mockery of the Constitution's deliberate choice to require clear and specific appointment of those wielding the executive power of the United States. Assuming proper appointment as officers of the Commission, SEC ALJ's conduct would be directly imputed to the Commission; the Commission could not then hide behind the pretense that ALJs are independent actors doing something other than wielding the Commission's power.

SUMMARY OF ARGUMENT

As both the Petitioners and the government persuasively argue, the *Lucia* panel misapplied this Court's long-standing, uninterrupted precedent for determining whether a government official's duties render him or her a constitutional officer who must be appointed in conformity with the Appointments Clause. *See* Pet'rs Br. at 26-33; Brief for Respondent Supporting Petitioners at 33-38, *Lucia v. SEC*, No. 17-130 (Feb. 21, 2018) ("Resp't Br."). Separately, the panel also incorrectly dismissed

clear congressional intent (expressed in plain statutory language as well as legislative history) that SEC ALJs must be properly-appointed constitutional officers. *See Raymond J. Lucia Cos. v. SEC*, 832 F.3d 277, 289 (D.C. Cir. 2016), *aff'd en banc by an equally divided court*, 868 F.3d 1021 (D.C. Cir. 2017). This *amicus* brief focuses on the second of those defects. The relevant statutes and their legislative histories demonstrate beyond doubt that Congress intended that Commission hearings be held by "Officers of the United States" only. As discussed below, Congress understood that it was delegating significant executive power to SEC ALJs and wanted that power to be wielded by people of rank and responsibility as insurance against abuses of power, and so that the public would view administrative proceedings as meaningful, competent, and fair. The panel's decision thwarts clearly expressed congressional language, understanding, and intent.

The *Lucia* panel's error in this respect can be traced directly to the SEC's argument below, which the panel adopted verbatim. The federal securities laws command that hearings "be held before the Commission or *an officer or officers of the Commission designated by it*," *see, e.g.*, 15 U.S.C. § 77u (emphasis added), yet the SEC consistently argued (until the government here conceded error below) that "there is no indication Congress intended these officers to be synonymous with 'Officers of the United States,'" *Raymond J. Lucia Cos.*, 832 F.3d at 289; *see also* Opinion of the Commission, *In re Raymond J. Lucia Cos.*, Admin. Proc. File No. 3-15006, 2015 WL 5172953, at *23 n.122 (Sept. 3, 2015). Congress's deliberate use of the words "officer or officers" is, of course, the best possible indication of that very intent, because the word "officer" is imbued with constitutional meaning. The relevant

legislative history is another good indication. Yet, the panel said nothing about the statutory interpretation points raised by the *amici*, nor did it address the legislative history demonstrating that Congress meant and understood that the terms "constitutional officers" and "officers" were synonyms. *See* Brief of Mark Cuban as *Amicus Curiae* in Support of Petitioners, *Raymond J. Lucia Cos.*, 832 F.3d 277 (Feb. 8, 2016) (No. 15-1345).

The panel's sole reference to congressional intent was its observation that it found no evidence of congressional intent "that the ALJ who presides at an enforcement proceedings [sic] be delegated the sovereign power of the Commission to make the final decision." *See Raymond J. Lucia Cos.*, 832 F.3d at 287 (emphasis added). This observation is incorrect because, as the government concedes, the statutory scheme does permit SEC ALJs to issue final decisions. Resp't Br. at 34. This observation is also beside the point, for it confuses *what* may be delegated with *to whom*. In any event, it is clear from the legislative history that Congress's intent was not dependent on delegation of power to issue final decisions; Congress required that hearings be held by constitutional officers because of the seriousness of the subject matter as well as the powers attendant to conducting them (and even gathering evidence in advance of them).

As the Director of the SEC's Division of Enforcement conceded in briefing the Commission on the same issue in one of the 13 matters that will be impacted by the Court's decision, *see* Pet'rs Br. at 48: "The Constitution assigns to Congress the authority to determine, in the first instance, whether a position it creates is that of an officer or of an employee, and '[t]hat constitutional assignment to Congress

counsels judicial deference.'" Division of Enforcement's Memorandum of Law in Response to the Commission's May 27, 2015 Order Requesting Supplemental Briefing, *In re Timbervest, LLC*, Admin. Proc. File No. 3-15519 (July 1, 2015) (first quoting U.S. Const. art. II , § 2, cl. 2, then quoting *In re Sealed Case*, 838 F.2d 476, 532 (D.C. Cir.) (Ginsburg, J., dissenting), *rev'd sub nom. Morrison v. Olson*, 487 U.S. 654 (1988)), https://www.sec.gov/litigation/apdocuments/3-15519-event-148.pdf.

When the securities laws and the APA are read together, both the statutes and the legislative histories unmistakably show that Congress intended that SEC ALJs had to be officers of the United States. This congressional determination is fully rational and merits acceptance, as evidenced by the fact that the Petitioners, the government, and most of the court of appeals judges who have analyzed the issue agree that SEC ALJs wield the power of constitutional officers.[5]

ARGUMENT

I. THE SECURITIES LAWS REQUIRE THAT OFFICERS HOLD SEC HEARINGS.

Congress chose the following language to authorize SEC hearings:

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5. *See Raymond J. Lucia Cos.*, 868 F.3d 1021 (*en banc* decision resulting in an equally divided court: 5-5); *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016) (panel decision resulting in two of three judges on the panel holding that SEC ALJs are constitutional officers).

> All hearings shall be public and may be held before the Commission or ***an officer or officers of the Commission designated by it*** . . . .

Securities Act of 1933, 15 U.S.C. § 77u (emphasis added).[6]

Plain language of legislation must be given its plain meaning. *Hardt v. Reliance Standard Life Ins. Co.*, 560 U.S. 242, 251 (2010) ("[W]e begin by analyzing the statutory language, 'assum[ing] that the ordinary meaning of that language accurately expresses the legislative purpose.' We must enforce plain and unambiguous statutory language according to its terms." (citations omitted)); *United States v. Germaine*, 99 U.S. 508, 510 (1878) (finding that when Congress uses the phrase "officers of the United States," it means constitutional officers and stating that an intent to describe someone other than a constitutional officer is denoted by words such as "servant, agent, person in the service or employment of the government"). Unless contrary intent is apparent, in other words, one must assume that Congress meant "officers" in the constitutional sense when it used the word "officers" for at least four reasons. First, the word "officer" is imbued with significant meaning in our constitutional framework—Article II, Section 2 of the Constitution itself refers to the "principal Officer in each of the executive Departments," "Officers of the United States," and "inferior Officers." U.S. Const. art. II, § 2; *see*

6. *See also* Securities Exchange Act of 1934, 15 U.S.C. § 78v ("Hearings . . . may be held before the Commission, any member or members thereof, or any officer or officers of the Commission designated by it . . . ."); Investment Advisers Act of 1940, 15 U.S.C. § 80b-12 (same); Investment Company Act of 1940, 15 U.S.C. § 80a-40 (same).

Buckley v. Valeo, 424 U.S. 1, 125-26 (1976). Second, this Court has expressly interpreted the phrase "officer of the United States" in legislation as meaning a constitutional officer, *see Germaine*, 99 U.S. at 510, and Congress's choice of that language should be deemed to incorporate the Court's interpretation, *see Jerman v. Carlisle, McNellie, Rini, Kramer & Ulrich LPA*, 559 U.S. 573, 589-90 (2010) ("[W]hen 'judicial interpretations have settled the meaning of an existing statutory provision, repetition of the same language in a new statute indicates, as a general matter, the intent to incorporate its . . . judicial interpretations as well.'" (citations omitted)). Third, the grouping of the Commission itself with its officers in this provision implies a parity of stature—*i.e.*, Congress's reference to "officers" is a reference to constitutional officers because they are equally empowered to "exercis[e] significant authority pursuant to the laws of the United States." *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 486 (2010) (quoting *Buckley*, 424 U.S. at 125-26). Finally, the word "designated" indicates that the Commission cannot empower someone who is not already an officer to serve in officer capacity for the purpose of holding a hearing; only someone who is already an officer—properly appointed and sworn in—may be *designated* to hold such a hearing.

II. LEGISLATIVE HISTORY OF THE SECURITIES LAWS CONFIRMS THAT CONGRESS USED THE WORD "OFFICER" TO MEAN CONSTITUTIONAL OFFICER.

The relevant legislative history confirms that Congress meant SEC hearings to be administered by constitutional officers.

A. The Legislative History of the Securities Act.

Empowering administrative agencies with significant adjudicatory powers was a significant undertaking in 1933. Indeed, at that time, the administrative state expanded rapidly, both through the creation of new agencies and the growth of established agencies. *See* Attorney Gen.'s Comm. on Admin. Procedures, U.S. Dep't of Justice, Final Report of Attorney General's Committee on Administrative Procedure 7-11 (1941) ("Attorney General's Committee Report"). In the 1930s alone, Congress created and authorized 17 federal agencies, including the SEC. *Id.* at 10. Congress, therefore, grappled not only with the particulars of what subject areas each federal agency would regulate and what shape those regulations should take, but also with the question of who should wield the newly-expanded powers of the executive branch. Put differently, Congress was intensely focused on which individuals within each agency should exercise certain powers and functions, and, therefore, Congress chose its words carefully.

With this as backdrop, congressional debate in connection with the House bill that eventually became the Securities Act of 1933 reflects deep concerns about vesting any non-judicial officer with the power to hold hearings, administer oaths and affirmations, compel attendance, and recommend severe sanctions. Indeed, initially there was even dissension as to whether the Commission itself and any of its members—all principal officers—should wield this power.

The initial House of Representatives' draft of the Securities Act of 1933 would have authorized the

Commission (then the Federal Trade Commission) to revoke a company's registration if, among other things, it found that the company was in "unsound condition." *See, e.g.*, H.R. 4314, 73d Cong. § 6 (1933). Certain members of Congress expressed concern that the power to take away someone's business because it was "unsound" was both unprecedented and immense. *See, e.g.*, *Federal Securities Act: Hearing Before the H. Comm. on Interstate & Foreign Commerce*, 73d Cong. 44-45 (1933) (Representative Clarence Lea described this power as "a rather radically different field" than the one of controlling publicity or disclosures).

To address these concerns, drafters initially proposed vesting such powers only in *principal* officers of the United States. For example, an early draft bill, H.R. 4314, placed officers empowered to act for the Commission on the same footing as Commission members who were principal officers. Specifically, the relevant draft language would have provided, in relevant part:

> SEC. 6. That the Commission may revoke the registration of any security by entering an order to that effect, if upon examination .... In making such examination ***the Commission or other officer or officers designated by it*** shall have access to and may compel the production of all the books and papers of such issuers.... ***The issuer or other person or entity applying for registration shall on application to the Commission within thirty days from the entry of such order be entitled to a public hearing***
> ....

H.R. 4314, 73d Cong. § 6 (1933) (emphasis added). Initial drafts of this legislation always contemplated that members of the Commission would be principal officers.[7] Therefore, the use of the word "other" to modify the words "officer or officers" suggests parity; reflecting congressional intent that investigations and hearings be conducted either by principal officers who are Commissioners or other principal officers designated by the Commission for that purpose.

Congress was concerned about vesting this amount of control and power *even* with the Commission or any other principal officer. In one illuminating exchange, Chairman Sam Rayburn, of the House of Representatives Committee on Interstate and Foreign Commerce, questioned Mr. Ollie Butler from the Department of Commerce, who participated in drafting the bill. Noting that "we have passed a lot of laws since we met here on the 5th of March, but I do not think we have given anybody that much power yet," Chairman Rayburn asked Mr. Butler: "If you were going to pass upon whether or not a man's business was based upon sound principles, you would want quite a corps of the ablest economists in the land to sit around you, would you not?" *Federal Securities Act: Hearing Before the H. Comm. on Interstate & Foreign Commerce*, 73d Cong. 135 (1933). After Mr. Butler conceded that "[i]t would be necessary to give an intelligent opinion on such a subject," Chairman Rayburn pressed his point, stating:

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7. Congress initially imbued the Federal Trade Commission with the authority to carry out the Securities Act of 1933. That Commission is "composed of five Commissioners, who shall be appointed by the President, by and with the advice and consent of the Senate." 15 U.S.C. § 41.

> Do you believe that ***an administrative officer of the Government*** ought to be given that much power, as a general principle—to pass upon whether or not a man's business is based on sound principles? It is mighty easy when you go to write a statute, if you want to delegate absolute authority; you can write that in a very short statute; but the question that this committee has got to determine is whether or not they want to give ***anybody*** that kind of authority. Is it your opinion, as a lawyer and as an economist, that the Federal Trade Commission, or a bureau in the Federal Trade Commission, or ***somebody at the head of a bureau in the Federal Trade Commission***, should be given the power to pass upon whether or not a man's business is based upon sound principles?

Id. (emphasis added).

When Mr. Butler conceded that the powers at issue were indeed very broad, Chairman Rayburn again asked whether such powers should be conveyed even to principal officers because, as he observed, those principal officers were only as good as Commission personnel:

> And yet we are committing them into the hands of a commission, of men appointed by the President, and, of course, confirmed by the Senate. But you know, as long as you have been around Washington—you will not have to stay here long to find out—that any law, the administration of which you commit to a

> board or commission, is just about as good in its administration, or as bad, ***as the personnel of the commission***. Therefore, if this commission could always be composed of men who were wise and men who were good, that would be one thing; but it is quite a hazard, is it not, realizing the personnel in the past of some of these commissions?

Id. at 135-36 (emphasis added); *see also Federal Securities Act: Hearings Before the S. Comm. on Banking & Currency*, 73d Cong. 103-04 (1933) ("That is quite a lot of power to give to an official, to determine that in his opinion a given enterprise is not based upon sound principles.").

Similarly, a related draft provision authorizing investigations and giving powers to compel production of evidence and take sworn testimony provided:

> For the purpose of all investigations . . . , ***the Commission and officer or officers designated by it*** are empowered to subpena [sic] witnesses, examine them under oath, and require the production of any books, papers, or other documents which the Commission deems relevant or material to the inquiry.

H.R. 4314, 73d Cong. § 15(b) (1933) (emphasis added).[8] Given the revocation-for-being-unsound debate context, the only reasonable interpretation of this language is that it too referred to constitutional officers.

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8. *Compare* 15 U.S.C. § 77s(c) (similar).

A later draft bill, H.R. 5480, narrowed draft Section 6 and removed the power to revoke registration of securities based on an unsound condition of an issuer. *See* H.R. 5480, 73d Cong. § 6 (1933). It allowed the Commission to enter a stop order suspending a registration statement if it appeared that the statement included any material false statements or omissions. *Id.* § 8(d). Additionally, it slightly modified the language regarding who was authorized to conduct stop order examinations by replacing the words "other officer" with the words "any officer." *Compare* H.R. 4314, 73d Cong. § 6 (1933), *with* H.R. 5480, 73d Cong. § 8(e) (1933) ("In making such examination the Commission or ***any*** officer or officers designated by it shall . . . ." (emphasis added)).

This modification shows two things: First, by replacing the word "other" with the word "any," the new draft provision empowered both inferior and principal officers. One can infer that once the drafters narrowed the grounds on which the Commission could revoke a registration, they were comfortable permitting inferior officers to hold examinations and exercise attendant powers. Second, this is a deliberate, considered change because it obviously changes the meaning of the provision. H.R. 5480 was passed on May 5, 1933. *See* 77 Cong. Rec. 2910-55 (1933).

The original Senate draft bill, S. 875, largely tracked the original House bill, H.R. 4314; it too included a clause that would have allowed revocation of a registration of an "unsound" business. *See* S. 875, 73d Cong. § 6(e) (1933). However, the Senate requested a Conference with the House. *See* H.R. 5480, 77 Cong. Rec. 2978-84, 2986-3000 (1933). The differences between the two chambers' bills

were reconciled in a Conference Report, and the final public law had three key parts:

(1) It retained the language in H.R. 5480 regarding the powers of "***the Commission or any officer or officers designated by it***" to examine witnesses under oath and require the production of documents in connection with a stop order examination. *See id.* at 3894 (emphasis added).

(2) It modified the language of H.R. 5480 regarding investigations, so that "***any member of the Commission or any officer or officers designated by it*** are empowered to administer oaths and affirmations, subpena [sic] witnesses, take evidence, and require the production" of documents for purposes of investigations. *See id.* at 3896 (emphasis added).[9]

(3) It added a section entitled "Hearings by Commission," directing that: "All hearings shall be public and may be held before ***the Commission or an officer or officers of the Commission designated by it*** . . . ." *See* 77 Cong. Rec. 3896-97 (1933) (emphasis added).

The Conference Report was subsequently agreed to by both the House and Senate. *Id.* at 3903, 4009 (1933).

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9. Note that "the Commission or officers" was replaced with "any member of the Commission or any officer or officers," indicating that Congress was focused on this provision. *Compare* H.R. 5480, 73d Cong. § 19(b) (1933), *with* 77 Cong. Rec. 3896 (1933).

In sum, Congress chose the word "officer" carefully and calibrated its grant of authority to executive officers based on the scope of delegated powers.

B. The Legislative History of the Securities Exchange Act.

The following year, Congress passed a companion act, the Securities Exchange Act of 1934. This act, of course, established the SEC. In it, Congress imbued the Commission and the officers it designated with certain executive functions, such as subpoenaing witnesses, administering oaths, and compelling the production of documents.

Notably, the initial version of the Senate bill included much of the same language and structure as the Securities Act on the relevant issues. That draft started by outlining the "Special Powers of the Commission" in Section 18:

> For the purpose of all investigations which, in the opinion of the Commission, are necessary and proper for the enforcement of this Act, ***any member of the Commission or any officer or officers designated by it are empowered to administer oaths and affirmations, subpena [sic] witnesses, compel their attendance, take evidence, and require the production of*** any books . . . .

S. 2693, 73d Cong. § 18(e) (1934) (emphasis added). As with the Securities Act, this was a grant of executive power to the Commission members and any *officers* designated by the Commission (and no one else).

Further edits to the relevant language suggest continued meticulous attention to detail, especially to the scope and nature of delegated powers. First, both the House and Senate edited the language so that it would cover not just investigations, but also "all inquiries." *See, e.g.*, H.R. 8575, 73d Cong. § 6(c) (1934); S. 3234, 73d Cong. § 6(c) (1934). Second, following the Conference Report (in which the Senate and the House versions were reconciled), this provision was further edited so that, in the enacted version of the law, these powers and privileges could be exercised by the Commission, any member of the Commission, or any officer of the Commission in relation to any investigation "or any other proceeding under this title." Securities Exchange Act of 1934, Pub. L. No. 73-291, § 21(b), 48 Stat. 881, 900; *see* 15 U.S.C. § 78u(b).

The attention to the wording of the provision authorizing hearings in the Exchange Act also indicates that Congress intended hearings to be held by constitutional officers. The draft provided:

> All hearings shall be public and may be held before the Commission, ***any member or members thereof*** or an officer or officers of the Commission designated by it, and appropriate records thereof shall be kept.

S. 2693, 73d Cong. § 21 (1934) (emphasis added). Note that the highlighted language was an addition to the language in the Securities Act's analogous provision, making it even more explicit that not all hearing officers needed to be principal officers, *i.e.*, Commission members or their peers. Apparently, having resolved (with the Securities Act's passage) that inferior officers could also

hold hearings, Congress added the highlighted language to reflect that. This change also emphasizes that, when conducting hearings, designated hearing officers wield equivalent powers as and enjoy parity of stature with individual Commission members, all of whom are principal officers. Congress's careful choice of who could wield the hearing-related powers it was delegating would be upended were one to read "employee" where Congress said "officer."[10]

Finally, Congress understood that the choice of the words "employee" or "officer" in the Exchange Act carried legal implications. For example, the use of the word "appoint" in Section 4, which establishes the Commission and authorizes it to employ staff, indicates that Congress

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10. Yet another reason to conclude that Congress meant that hearings be held by officers of the United States is the use of the word "officer" in the Exchange Act provision for cases of contumacy or refusal to comply with Commission subpoenas. Under that provision, too, the federal courts would only be able to order a person to appear before the Commission, one of its members, or any officer of the Commission. *See* 15 U.S.C. § 78u(c). However, this provision of the Exchange Act is slightly different than a similar provision of the Securities Act and different in a manner that confirms Congress's intent that hearings be held before constitutional officers. In the Exchange Act, the words "or member or officer designated by the Commission" replace the words "one of its examiners designated by it" in the Securities Act. *Compare* 15 U.S.C. § 78u(c) (Exchange Act), *with id.* § 77v(b) (Securities Act). Two things follow from this change: one, the choice of the word "officer" was deliberate; and two, because these are two references to the same individuals, Congress used the word "examiners" in the Securities Act as a descriptive term for all officers who were designated to conduct hearings or investigations, including, of course, Commission members.

was sensitive to the significance of the term "officer."[11] Specifically, initial House and Senate drafts did not authorize the Commission to "appoint" officers or anyone else. *See, e.g.*, H.R. 7924, 73d Cong. § 3 (1934); S. 2642, 73d Cong. § 4(e) (1934) (initial Senate draft: "The Commission is further authorized, in accordance with the civil service laws, to employ . . . such officers and employees . . . as may be necessary . . . ."). The addition of the word "appoint" in the enacted law signified that Congress understood that the Commission needed authority to appoint certain of its employees to "officer" positions.[12] There is no other reason to change "employ" to "appoint."

In sum, as this legislative history establishes, Congress painstakingly considered the administrative scheme it was creating and to whom it would convey certain executive authority, making a constitutional determination that only officers wield executive power.

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11. Section 4(b) of the final enacted law reads, in relevant part: "The Commission is authorized to appoint and fix the compensation of such officers, attorneys, examiners, and other experts as may be necessary . . . and the Commission may . . . appoint such other officers and employees as are necessary . . . ." *See* Securities Exchange Act of 1934, Pub. L. No. 73-291, § 4(b), 48 Stat. 881, 885.

12. The current provision is: "The Commission shall appoint and compensate officers, attorneys, economists, examiners, and other employees in accordance with section 4802 of title 5." 15 U.S.C. § 78d(b)(1).

III. CONGRESS INTENDED SEC ALJS TO BE PROPERLY APPOINTED CONSTITUTIONAL OFFICERS UNDER THE APA.

The relevant language and legislative history of the APA also display clear congressional intent to have SEC hearings held by, at minimum, inferior officers of the United States. Indeed, following lengthy discussions and analysis, the APA left the appointment of hearing officers to the heads of departments that selected them precisely because Congress recognized that, as inferior officers, these hearing examiners had to be appointed in a manner consistent with the Appointments Clause.

A. The APA Also Places ALJs on the Same Footing with Principal Officers.

In parallel with the placement of hearing officers on par with the Commission members in the securities laws, the APA also places ALJs on par with heads of departments, *i.e.*, principal officers: "There shall preside at the taking of evidence—(1) the agency; (2) one or more members of the body which comprises the agency; or (3) one or more administrative law judges appointed under section 3105 of this title." *See* 5 U.S.C. § 556(b). As the discussion below shows, this was no accident; this language reflects Congress's policy choices and careful analysis.

B. Empowerment of ALJs Was a Reaction to Earlier Functioning of Administrative Agencies.

The APA stemmed from a review of administrative agencies following the expansion of the administrative state after the Great Depression. *See generally* Attorney General's Committee Report; *see also* S. Comm. on the Judiciary, 79th Cong. Admin. Procedure (Comm. Print 1945), S. Doc. No. 79-248, at 11-42 (1944-46); Attorney Gen.'s Comm. on Admin. Procedure, U.S. Dep't of Justice, U.S. Sec. & Exch. Comm. (Monograph 26) 189 (1940) (describing hearing practices at the SEC and criticizing the SEC for the impression, whether real or perceived, that it withheld real power from its hearing examiners).[13] The APA was meant to elevate all hearing officers (including, specifically, SEC hearing examiners) in order to address some of the concerns raised about the early years of the administrative state. The Attorney General's Committee Report outlined certain procedural and substantive defects in the then-current administrative functions, including in formal adjudications, and provided a proposed draft of the APA. *See generally* Attorney General's Committee Report at 7-25, 191-203. The concerns raised in the Report animated the passage of the APA and informed much of its language.

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13. In 1978, Congress amended the United States Code to change the title of "hearing examiners" to "Administrative Law Judges" and to increase the number of such positions at the GS-16 level. Act of Mar. 27, 1978, Pub. L. No. 95-251, 92 Stat. 183, 183-84.

The Committee recommended that:

- Agency heads delegate much of the investigatory and prosecutorial functions to capable officers and the initial adjudicative functions to other independent officers. *See id.* at 46, 55-60.

- The status of all hearing officers be elevated to allow them to command public confidence and exercise "functions of responsibility and interest." *Id.* at 43-44, 46.

- The hearing officers' initial decisions be given real weight, *i.e.*, the initial decision would become final absent clear error. *Id.* at 50-51 ("In general, the relationship upon appeal between the hearing commissioner and the agency ought to a considerable extent to be that of trial court to appellate court.").

- Congress empower the hearing officers to exercise certain executive or sovereign functions, such as "preside at hearings, issue subpoenas, administer oaths, rule upon motions, carry out other duties incident to the proper conduct of hearings, and make findings of fact, conclusions of law, and orders for the disposition of matters coming before them." *Id.* at 50.

- To attract and appoint "men of ability and prestige," the agency should have an important role in selecting and appointing the hearing officers, but also an independent body should be in charge of investigating and approving that person's qualifications:

> [T]he hearing commissioner is in a very real sense acting for the head of the agency. He is hearing cases because the heads cannot as a practical matter themselves sit. . . . The entire usefulness of the agency may be destroyed if the hearing officers are incompetent or if the public loses confidence in their fairness. . . [But] before anyone should ***undertake these highly responsible duties of a hearing commissioner*** his judicial qualifications and capacity should be investigated and approved by a body independent of the agency.

Id. at 46-47 (emphasis added).

These recommendations, according to the Committee, were necessary to assure that administrative proceedings were a fair method of dispute resolution. As the Committee stated:

> The Committee believes that its recommendations in the preceding chapter for the conduct of hearings by able, independent, ***and responsible*** hearing commissioners will do much to assure these fundamentals of a fair hearing.

Id. at 68 (emphasis added).

C. Congress Intended ALJs to Be "Presiding Officers," Appointed in Accordance with the Appointments Clause.

Acting on the above-described prescriptions, Congress passed the APA, which, as detailed below: (1) made the

hearing examiners "presiding officers"; (2) granted them certain executive powers; (3) mandated that the decisions of subordinate officers be given weight and force; and (4) made certain that the appointment of ALJs are made in conformity with the Appointments Clause.

1. Congress referred to hearing examiners as "presiding officers."

Congress referred to hearing examiners as "presiding officers" in the original legislation:

> SEC. 7. In hearings which section 4 or 5 requires to be conducted pursuant to this section—
>
> (a) ***PRESIDING OFFICERS.***—There shall preside at the taking of evidence (1) the agency, (2) one or more members of the body which comprises the agency, or (3) one or more examiners appointed as provided in this Act . . . . The ***functions of all presiding officers and of officers participating in decisions*** in conformity with section 8 shall be conducted in an impartial manner.

Administrative Procedure Act of 1946, Pub. L. No. 79-404, § 7(a), 60 Stat. 237, 241-42 (emphasis added). Parallel to the Exchange Act, this provision covered three categories of persons: the Commission acting together, individual Commissioners, and other persons appointed to hold hearings. The words "the functions of all presiding officers" referred to all three of these categories. The sole sensible reading of this language is that the grouping of examiners with principal officers in this section indicates that examiners should have officer status.

The very next provision of the APA as originally adopted supports this reading. It states:

> (b) ***Hearing powers.—Officers presiding at hearings shall have authority***, subject to the published rules of the agency and within its powers, to (1) administer oaths and affirmations, (2) issue subpenas [sic], ... and (9) take any other action authorized by agency rule consistent with this Act.

Id. § 7(b), 60 Stat. 237, 242 (emphasis added). When acting as hearing examiners, the agency, any of its individual members, or any other presiding officer appointed under the APA could wield equivalent executive power under this provision, suggesting status parity.

2. The statutory definitions of "officer" and "employee" confirm that Congress intended SEC ALJs to be "inferior officers."

In 1965, in connection with the adoption of the revised Title 5, Congress restated "in comprehensive form, without substantive change, the statutes in effect before July 1, 1965, that relate to Government employees, the organization and powers of Federal agencies generally, and administrative procedure . . . ." H.R. Rep. No. 89-901, at 1 (1965). Congress made language changes to streamline and standardize terms across various interrelated statutory provisions without changing their meaning. *Id.* at 2-3.

Among other things, Congress defined the terms "officer" and "employee" in new Sections 2104 and 2105,

respectively. *See generally id.* at 8, 10, 12-13. Applying these definitions, Congress amended the hearing-authorizing provisions of the APA thus:

> The words "employee" and "employees" are substituted [in Section 556(b)] for "officer" and "officers" ***in view of the definition of "employee" in section 2105.*** The sentence "A presiding or participating employee may at any time disqualify himself[,]" is substituted for the words "Any such officer may at any time withdraw if he deems himself disqualified."

Id. at 13 (emphasis added).

Similar changes and qualifying comments were made in Section 557. *Id.* By noting that the substitution of "employee" for "officer" was made in view of the expansive definition of "employee," Congress indicated that it understood that "officer" and "employee" were not interchangeable terms and that, therefore, as originally drafted, officer did not mean employee. *See id.* An analysis of these definitions shows that SEC ALJs are officers under the APA.

"Officer" is defined thus:

> (a) For the purpose of this title, "officer", except as otherwise provided by this section or when specifically modified, means a justice or judge of the United States and ***an individual who is***—
>
> (1) ***required by law to be appointed*** in the civil service ***by*** one of the following acting in an official capacity—

(A) the President;
(B) a court of the United States;
(C) ***the head of an Executive agency***; or
(D) the Secretary of a military department;

(2) engaged in the performance of a Federal function under authority of law or an Executive act; and

(3) subject to the supervision of an authority named by paragraph (1) of this section, or the Judicial Conference of the United States, while engaged in the performance of the duties of his office.

5 U.S.C. § 2104 (emphasis added).

"Employee" is defined thus:

(a) For the purpose of this title, "employee", except as otherwise provided by this section or when specifically modified, ***means an officer*** and an individual who is—

(1) appointed in the civil service by one of the following acting in an official capacity—

(A) the President;
(B) a Member or Members of Congress, or the Congress;
(C) a member of a uniformed service;
(D) an individual who is an employee under this section;
(E) the head of a Government controlled corporation; or

> (F) an adjutant general designated by the Secretary concerned under section 709(c) of title 32;
>
> (2) engaged in the performance of a Federal function under authority of law or an Executive act; and
>
> (3) subject to the supervision of an individual named by paragraph (1) of this subsection while engaged in the performance of the duties of his position.

5 U.S.C. § 2105 (emphasis added). In other words, the "employee" definition automatically includes all officers (both principal and inferior) as well as certain non-officers falling within subsections (a)(1), (a)(2), and (a)(3).

Indeed, the only reason that SEC ALJs meet the statutory definition of "employee" in Section 2105 is that they meet the statutory definition of "officer" in Section 2104. SEC ALJs are not covered by subsections (a)(1) and (a)(3) of Section 2105 because they must be designated by the Commission under the securities laws (as discussed above) and, under the APA, they must be appointed by the "agency." *See* 5 U.S.C. § 3105 ("Each agency shall appoint as many administrative law judges as are necessary for proceedings required to be conducted in accordance with sections 556 and 557 of this title."). In other words, SEC ALJs do not meet Section 2105's tests for non-officer employees. But, SEC ALJs are "officers" under Section 2104 because they (1) must be appointed by the Commission; (2) perform their duties under authority of law; and (3) are subject to supervision by the head of

an executive agency—the Commission.[14] Accordingly, because they are officers under Section 2104, they also are "employees" under the preambular language of Section 2105(a).

D. Congress Explicitly Made Certain that ALJs' Appointments Complied with the Appointments Clause.

To dispel any lingering doubt about congressional intent in using the word "officer" to mean "inferior officer" of the United States when referring to ALJs in the APA, Congress directly addressed whether hearing officers had to be appointed in conformity with the Appointments Clause. Its answer was yes. This was an explicit recognition by Congress that hearing officers are meant to be inferior officers.

The Attorney General's Committee Report recommended that hearing officers be appointed by an independent government body. Attorney General's Committee Report at 47-49. To accomplish this, the Committee recommended the formation of an "Office of Administrative Justice," whose Director would be appointed by the Judicial Conference and who would, in turn, appoint hearing examiners. S. Comm. on the Judiciary, 79th Cong. Admin. Procedure (Comm. Print 1945), S. Doc. No. 79-248, at 41-42 (1944-46).

---

14. The SEC is an Executive agency. *See* 5 U.S.C. § 101-105; *see also Free Enter. Fund*, 561 U.S. at 512-13 (the Commission acting together is the head of an agency.).

This proposal was rejected because it ran afoul of the Appointments Clause. As explained by the Senate Judiciary Committee:

> The legal difficulty with the suggestion, however, is that the ***Constitution provides for the placing of powers of appointment*** "in the courts of law" whereas the Judicial Conference is a committee and not a court and hence may ***not be within the constitutional authorization for appointing powers.***

Id. at 42 (emphasis added).

The same concerns were voiced in the House hearings. The then-President of the American Bar Association (ABA) testified that the Judicial-Conference-Appointment proposal may present constitutional appointment power problems. *Id.* at 50. The Chairman of the Special Committee on Administrative Law for the ABA concurred:

> The third proposal has been made recently, and that is that either the selection or the approval of the examiner be vested in some official appointed by the Judicial Conference. . . . However, ***that presents a very serious constitutional question as to whether you could have the Judicial Conference make the appointment of an executive official when the Constitution vests the power of appointment only in the President, the head of a department[, or] a court.*** The Judicial Conference is not a court.

Id. at 82 (emphasis added).

To address this issue, Congress made certain the proposed bill complied with the Appointments Clause. The next suggestion taken up (and ultimately adopted) by the Senate Judiciary Committee was that the "examiners be appointed '*by* each agency' rather than [just] 'for each agency.'" *Id.* at 42 (emphasis in original). In those instances where agency heads are heads of departments, such as the SEC, this change ensured proper Article II appointments. *See Free Enter. Fund*, 561 U.S. at 511 (SEC constitutes a department).

E. Congress Was Conferring Significant Executive Powers in the APA.

Were Congress not conferring significant executive powers on ALJs, it would not have bothered with the Appointments Clause. The following comment from the Senate Judiciary Committee is illuminating:

> It has been suggested that this bill should grant the subpena [sic] power to all hearing officers, ***whether or not the agency has been granted such power***. It may seem logical that hearing officers should have compulsory process powers, but it has been felt that the grant of such powers is of such a nature and so important as to be better left to Congress in connection with specific legislation rather than dealt with by a general statute.

S. Comm. on the Judiciary, 79th Cong., Admin. Procedure (Comm. Print 1945), S. Doc. No. 79-248, at 29-30 (1944-46) (emphasis added). There would be no reason to consider giving ALJs *independent* subpoena powers if Congress

meant them to be mere employees whose job was limited to serving as aides to the Commission. Note that the decision not to vest ALJs with independent subpoena power did not rest on their status as mere employees or aides. Rather, Congress saw the delegation of subpoena power to be significant enough to require a specific statutory grant. *A fortiori*, exercise of subpoena powers by SEC ALJs is exercise of significant executive power.

To be sure, the original APA text distinguished between supervising officers and subordinate officers, but that distinction is most naturally read as tracking the Constitution's distinction between principal and inferior officers, because every inferior officer, by definition, is subordinate to, and is subject to supervision by, a principal officer. In referring to subordinate examiners, therefore, Congress repeatedly used the word "officer." *See* Administrative Procedure Act of 1946, Pub. L. No. 79-404, § 8, 60 Stat. 237, 242-43.

In short, Congress empowered ALJs carefully and in full recognition of the importance of officer status to their functions. As the Senate Judiciary Committee explained, the APA was "designed to assure that the presiding officer will perform a real function rather than serve merely as a notary or policeman." S. Rep. No. 79-752, S. Doc. No. 79-248, at 207, 269. Similarly, the Chairman of the Senate Judiciary Committee, Pat McCarran, wrote that the APA "is intended as a guide to him who seeks fair play and equal rights under law, as well as to those invested with executive authority." S. Comm. on the Judiciary, 79th Cong., Admin. Procedure (Comm. Print 1945), S. Doc. No. 79-248, at III (1944-46).

CONCLUSION

Both the relevant statutory language and legislative history show that Congress intended SEC ALJs to be inferior officers in the constitutional sense. Congress deliberately delegated significant executive powers to them. Recognizing the significance of the powers ALJs wield, Congress also made sure that their appointments comport with the Appointments Clause. The panel decision was incorrect, therefore, in dismissing statutory language and ignoring legislative history confirming congressional intent that SEC ALJs be properly appointed officers. SEC ALJs must be appointed in accordance with constitutional and congressional mandates.

Respectfully submitted,

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February 28, 2018

EXHIBIT

Redacted with

EXHIBIT — SUBPOENA AD TESTIFICANDUM OF THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION, DATED MARCH 14, 2014

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-15574

In the Matter of

HARDING ADVISORY LLC and

WING F. CHAU,

Respondents.

SUBPOENA AD TESTIFICANDUM

To: Michael Edman

[redacted]

Redacted with Redactit

YOU ARE HEREBY REQUIRED to appear before the Honorable Cameron Elliot, Administrative Law Judge of the Securities and Exchange Commission, at Room 238 of the Javits Federal Building, 26 Federal Plaza, New York, NY, on the 31st day of March 2014, or at any date thereafter, at 9:30 a.m., to provide testimony in the Matter of Harding Advisory LLC and Wing F. Chau, AP File No. 3-15574, a public administrative proceeding pursuant to the Section 8A of the Securities Act of 1933, Sections 203(e), 203(f), and 203(k) of the Investment Advisers Act of 1940, and Section 9(b) of the Investment Company Act of 1940.

IN TESTIMONY WHEREOF, the undersigned, an officer designated by the Securities and Exchange Commission, has hereunto set his hand at Washington, D.C.

Date: 3-14-2014

Signed: [signature]

Honorable Cameron Elliot
Administrative Law Judge

No. 17-130

IN THE
Supreme Court of the United States

RAYMOND J. LUCIA, ET AL.,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF CONSTITUTIONAL AND ADMINISTRATIVE LAW SCHOLARS AS *AMICI CURIAE* IN SUPPORT OF AFFIRMANCE

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INTEREST OF *AMICI CURIAE*[1]

Amici are law professors who teach or have taught courses in constitutional and administrative law and whose scholarship has devoted significant attention to the separation of powers, including Article II's Appointments Clause.

A full listing of *amici* appears in the Appendix.

SUMMARY OF ARGUMENT

The Securities and Exchange Commission (SEC) is an independent agency tasked by Congress with regulating the nation's securities markets. To assist the five-member Commission with its myriad responsibilities, Congress has permitted the Commission to "delegate, by published order or rule, any of its functions to . . . an administrative law judge." 15 U.S.C. § 78d-1(a). Administrative law judges (ALJs) are civil servants who are hired through a competitive process. *See* Vanessa K. Burrows, Cong. Research Serv., RL34607, *Administrative Law Judges: An Overview* 2-4 (2010). Although the Commission has chosen to delegate the tasks of holding hearings and drafting initial decisions in agency adjudications to ALJs, it has retained the authority to review any initial decision *de novo*, and no ALJ initial decision becomes binding without an express order of the Commission.

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[1] The parties have consented to the filing of this brief and their letters of consent have been filed with the Clerk. Under Rule 37.6 of the Rules of this Court, *amici* state that no counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amici* or their counsel made a monetary contribution to its preparation or submission.

Petitioners challenge the method by which ALJs are hired, arguing that ALJs are "Officers of the United States" under the Constitution's Appointments Clause, and that they therefore must be appointed by the President, a Court of Law, or the Head of a Department, rather than through a competitive hiring process. *See* U.S. Const. art. II, § 2, cl. 2. Petitioners' argument distorts the meaning of the Appointments Clause, contravenes over two centuries of practice, and threatens substantial disruption to the federal government's operations.

As this Court has emphasized, the Appointments Clause "is among the significant structural safeguards of the constitutional scheme," *Edmond v. United States*, 520 U.S. 651, 659 (1997), guarding against "congressional encroachment" and "ensur[ing] public accountability," *id.* at 659-60, by "preventing the diffusion of the appointment power," *Freytag v. Comm'r*, 501 U.S. 868, 878 (1991). Yet at the same time the Framers sought to accomplish these goals, they also sought to ensure that Congress would have flexibility in crafting the structure of the government and who works within it. *See* U.S. Const. art. I, § 8, cl. 18. This flexibility is apparent in the Appointments Clause's text, which grants Congress power to "vest the Appointment of . . . inferior Officers . . . in the President alone, in the Courts of Law, or in the Heads of Departments," as Congress "think[s] proper." *Id.* art. II, § 2, cl. 2. Moreover, as this Court has long recognized, the vast majority of federal government employees are "lesser functionaries" who fall outside the Appointments Clause's scope and whose method of appointment Congress has substantial discretion to determine. *See Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 506 n.9 (2010).

Congress has exercised this flexibility from the first days of the Republic to the present, consistently choosing to imbue some federal employees with significant responsibilities without requiring them to be appointed in the manner prescribed for constitutional "Officers of the United States." The First Congress, for example, passed statutes that created such positions as deputy marshal and customs inspector; these officials had important responsibilities, but were not appointed by the President, a Court of Law, or the Head of a Department. Notably, these early non-Officer employees shared many characteristics with modern ALJs: they assisted Officers with important statutory responsibilities, but they were always agents of, and therefore subordinate to, those Officers.

In 1946, with the growth of the modern administrative state, Congress passed the Administrative Procedure Act (APA) and created the position of hearing officer—the antecedent to today's ALJ—to assist federal agencies with their myriad regulatory and adjudicative responsibilities. *See* Pub. L. No. 79-404, § 11, 60 Stat. 237, 244. Though hearing officers, and subsequently ALJs, had the significant responsibilities of holding hearings and drafting initial decisions, agencies retained the sole authority to issue final, binding orders, and so ALJs themselves were not considered to be "Officers of the United States." *See generally Attorney General's Manual on the Administrative Procedure Act* 83 (1947) ("*Attorney General's Manual*") (noting that under the APA, an agency "is in no way bound by the decision" of a hearing officer and "retains complete freedom of decision—as though it had heard the evidence itself").

Despite these numerous examples dating back to the nation's birth, Petitioners insist that ALJs must be constitutional "Officers" because of their "substantive

and procedural powers that require the exercise of broad discretion," Pet'rs Br. 21. But the Appointments Clause is not concerned with "day-to-day discretion." *Bandimere v. SEC*, 844 F.3d 1168, 1197 (10th Cir. 2016) (McKay, J., dissenting). After all, "it is an everyday occurrence in the operation of government for staff members to conceive and even carry out policies for which duly appointed or elected officials take official responsibility." *Andrade v. Regnery*, 824 F.2d 1253, 1257 (D.C. Cir. 1987). Rather, to decide whether an employee is an "Officer," courts must engage in a case-by-case inquiry that asks whether the employee is "exercising significant authority" in his or her own right, or is rather a "lesser functionar[y] subordinate to officers," *Buckley v. Valeo*, 424 U.S. 1, 126 & n.162 (1976), who supervise that employee and will be held accountable for that employee's actions.

At every turn, ALJs are lesser functionaries subordinate to, and subject to the control of, the SEC. Though ALJs conduct hearings, their "initial decision[s]" are not final, let alone binding, *see* 17 C.F.R. § 201.360(a)(1) & (d), and any ALJ "decision becomes final" only "upon issuance of [an] order" by the Commission, *id.* § 201.360(d)(2). Moreover, the Commission reviews the initial decisions of ALJs *de novo*, Pet. App. 91a, and may, "[u]pon its own motion or the motion of a party, . . . allow the submission of additional evidence," 17 C.F.R. § 201.452. Finally, because only orders of the Commission have any binding effect, only orders of the Commission may form the basis of a challenge in an Article III court. *See* 15 U.S.C. § 77i(a). For all these reasons, ALJs are not constitutional "Officers," and they need not be hired in the manner prescribed by the Appointments Clause.

Were this Court to conclude otherwise, the disruption to the operations of the federal government could

be substantial, throwing into question the constitutionality of merit-based hiring for thousands of ALJs and non-ALJ administrative judges in other agencies, as well as other civil servants with significant responsibilities.[2] After all, if the linchpin of Petitioners' analysis is the mere existence of day-to-day responsibility and discretion—without taking into consideration whether employees are agents of, or subordinate to, Officers—their theory would seemingly encompass a large portion of the federal workforce. Such a profound expansion in the category of constitutional "Officers" would not only contravene longstanding precedent and practice, it would also undercut the Appointments Clause's goal of accountability by encouraging *pro forma* appointments. That cannot be right.

ARGUMENT

I. CONGRESS ENJOYS BROAD AUTHORITY TO SHAPE THE STRUCTURE OF THE FEDERAL GOVERNMENT, INCLUDING THE DISCRETION TO DETERMINE HOW TO APPOINT FEDERAL EMPLOYEES SERVING AS AGENTS OF, OR SUBORDINATE TO, OFFICERS.

1. When the Framers drafted the Constitution, they gave Congress broad flexibility to determine how best to shape the federal government. Although the Constitution presupposes the existence of federal "Departments," *see* U.S. Const. art. II, § 2, cl. 1, it does not specify what those Departments are, how they are to be organized, or who is to work within them. Likewise,

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[2] *Amici* use the term "civil servants" colloquially to refer to federal government employees hired based on merit, as opposed to political Officers.

while the Framers recognized that there would be "Officers of the United States" whom the President must appoint with the advice and consent of the Senate and "inferior Officers" whose appointment Congress could "vest . . . in the President alone, in the Courts of Law, or in the Heads of Departments," *id.* art. II, § 2, cl. 2, they did not specify in detail the characteristics that distinguish principal Officers from inferior Officers, or inferior Officers from other employees of the federal government.

This decision to leave open most questions about the structure of the federal government was no accident. The Constitutional Convention specifically rejected a plan that would have delineated in the Constitution itself the roles of specific executive departments. *See* 2 *The Records of the Federal Convention of 1787*, at 335-36 (Max Farrand ed., 1911) (proposal specifying duties of six department secretaries). Instead the Framers gave Congress the authority to "make all Laws which shall be necessary and proper for carrying into Execution the . . . Powers vested by this Constitution in the Government of the United States." U.S. Const. art. I, § 8, cl. 18.

The Necessary and Proper Clause "is the one and only provision of the Constitution that directly addresses the establishment of the federal government," and it "gives the relevant power expressly to Congress." John F. Manning, *Separation of Powers As Ordinary Interpretation*, 124 Harv. L. Rev. 1939, 1986 (2011). Under the Constitution, therefore, "Congress has plenary control over the salary, duties, and even existence of executive offices," *Free Enter. Fund*, 561 U.S. at 500, wielding broad authority over the structure of federal agencies and the Officers and employees who work within them.

2. Of course, Congress wields this power to shape the government subject to constitutional requirements, including the Appointments Clause. *See Buckley*, 424 U.S. at 138-39. But in giving Congress flexibility, the Framers also gave it considerable discretion to determine how the new government's functionaries would be selected.

The Appointments Clause provides that the President "shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for and which shall be established by Law." U.S. Const. art. II, § 2, cl. 2. Yet it allows Congress to "by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments." *Id.* Moreover, this Court has long recognized that "[one] 'may be an agent or employ[ee] working for the government and paid by it . . . without thereby becoming its officer[].'" *United States v. Germaine*, 99 U.S. 508, 509 (1878); *United States v. Maurice*, 26 F. Cas. 1211, 1214 (C.C.D. Va. 1823) (Marshall, C.J.) ("Although an office is 'an employment,' it does not follow that every employment is an office.").

To determine whether any given employee is an "Officer," this Court has insisted on a case-by-case inquiry that examines whether a given administrative structure grants that employee significant authority in his or her own right, or instead makes him or her subordinate to, or an agent of, an "Officer." In *Buckley*, for example, this Court identified an "Officer" as "any appointee exercising significant authority pursuant to the laws of the United States," 424 U.S. at 126, but also made clear that "lesser functionaries" who act

"subordinate to officers of the United States" are non-Officers and not subject to the Appointments Clause's requirements, *id.* at 126 n.162. Other decisions have articulated additional relevant features, such as whether the positions involve the "exercise [of] significant discretion," final decision-making power, *Freytag*, 501 U.S. at 881-82, "continuing and permanent" duties, or regular payment, *Germaine*, 99 U.S. at 511-12.

In the 1879 decision *United States v. Germaine*, this Court held that civil surgeons appointed by the Commissioner of Pensions "to make the periodical examination of pensioners which are or may be required by law, and to examine applicants for pension" were not "Officers" under Article II. 99 U.S. at 508 (quoting Act of March 3, 1873, ch. 234, 17 Stat. 576). In reaching that conclusion, this Court considered the "occasional and intermittent" nature of a civil surgeon's duties and the fact that Congress did not require that civil surgeons be appointed in conformity with Appointments Clause procedures. *Id.* at 511-12. Importantly, the Court also underscored that the surgeon is "but an *agent* of the commissioner . . . to procure information needed to aid in the performance of [the commissioner's] own official duties." *Id.* at 512 (emphasis added). Indeed, the Court noted that "[t]he surgeon is only to act when called on by the Commissioner of Pensions in some special case, as when some pensioner or claimant of a pension presents himself for examination." *Id.* Thus, despite the civil surgeons' significant responsibilities in helping to determine who could receive a pension, their status as agents of the Commissioner meant they were not constitutional "Officers." *Id.*; *see United States v. Mouat*, 124 U.S. 303, 307 (1888) (reaffirming *Germaine*).

Because "lesser functionaries" who act as agents of, and subordinate to, Officers are not themselves constitutional Officers, this Court has long recognized that non-Officers make up the vast bulk of the federal workforce. In 1878, the Court posited that "nine-tenths of the persons rendering service to the government undoubtedly" fell into this non-Officer category, *Germaine*, 99 U.S. at 509, and the Court recently noted that "[t]he applicable proportion has of course increased dramatically since [then]," *Free Enter. Fund*, 561 U.S. at 506 n.9.

This view that "lesser functionaries" who act "subordinate to officers of the United States" are non-Officers not only has a long vintage in this Court's precedents, it is also reflected in practices dating back to the nation's birth, as the next Section discusses.

II. THROUGHOUT THE NATION'S HISTORY, CONGRESS HAS GRANTED SIGNIFICANT RESPONSIBILITIES TO NON-OFFICERS SO LONG AS THEY ACTED AS AGENTS OF, OR SUBORDINATE TO, OFFICERS.

As this Court has repeatedly reaffirmed, "'[l]ong settled and established practice is a consideration of great weight in a proper interpretation of constitutional provisions' regulating the relationship between Congress and the President." *N.L.R.B. v. Noel Canning*, 134 S. Ct. 2550, 2559 (2014) (quoting *The Pocket Veto Case*, 279 U.S. 655, 689 (1929)); *see McCulloch v. Maryland*, 17 U.S. 316, 401 (1819) (courts "ought to receive a considerable impression" from "the practice of the government").

Recognizing this, Petitioners place weight on examples in which Congress has required seemingly low-level federal employees to be appointed in conformity with the Appointments Clause. *See* Pet'rs Br. 17-18.

But "the Appointments Clause does not prevent Congress from treating a position that is not, in the constitutional sense, an office under the United States as nevertheless subject to statutory restrictions on offices or officers." *Officers of the United States Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73, 116 (2007); *cf. Weiss v. United States*, 510 U.S. 163, 182 (1994) (Souter, J., concurring) (Congress may "decline[] to adopt the less onerous appointment process available for inferior officers" and instead require them to be "appointed in the manner of principal officers").[3] For that reason, the positions for which Congress has required Article II appointment procedures are less indicative of the Appointments Clause's scope than positions for which Congress has *not* required Article II appointment procedures.

It is therefore noteworthy that from the early days of the Republic through the modern era, Congress has assigned significant responsibilities to some federal employees *without* requiring that they be appointed via the Appointments Clause. In all of these areas, the employees acted as agents of, or subordinate to, other Officers and were therefore not considered to be "Officers of the United States" despite the significance of their day-to-day responsibilities.

1. The First Congress created "deput[ies]" for numerous public officials and assigned these deputies significant responsibilities as agents of their principals, yet did not require that they be appointed in the manner required by the Appointments Clause. *See*

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[3] For example, although most of the more than 240,000 active military officers are inferior Officers under the Appointments Clause, they are appointed in the manner of principal officers because Congress concluded that such appointment was preferable as a policy matter. *Weiss*, 510 U.S. at 182 (Souter, J., concurring).

Harmelin v. Michigan, 501 U.S. 957, 980 (1991) (opinion of Scalia, J.) ("actions of the First Congress" are "persuasive evidence of what the Constitution means").

For example, the First Judiciary Act of 1789 created the position of "marshal" for each judicial district and empowered the marshal "to appoint as there shall be occasion, one or more deputies, who shall be removable from office by the judge of the district court, or the circuit court sitting within the district, at the pleasure of either." An Act to Establish the Judicial Courts of the United States, ch. 20, § 27, 1 Stat. 73, 87 (1789). These deputies were, like marshals themselves, "bound for the faithful performance" of the marshal's duties—namely, "to attend the district and circuit courts when sitting therein," "to execute throughout the district, all lawful precepts directed to him," and "to command all necessary assistance in the execution of his duty." *Id.* Moreover, deputies—like marshals—were required to take an oath of office that they would "faithfully execute all lawful precepts directed to the marshal of the district . . . under the authority of the United States, and true returns make, and in all things well and truly, and without malice or partiality, perform the duties of the office of marshal (or marshal's deputy, as the case may be)." *Id.* Finally, the Act provided that "in case of the death of any marshal, his deputy or deputies *shall continue in office*, unless otherwise specially removed; *and shall execute the same* in the name of the deceased, until another marshal shall be appointed and sworn." *Id.* § 28, 1 Stat. at 87 (emphasis added).

As the statute says, then, the deputy to a U.S. marshal was given significant responsibility to carry out all of the marshal's statutory duties and even took over the marshal's role upon his death until a successor was

appointed. Moreover, the First Judiciary Act referred to the "marshal's deputy" as an "office" with "duties," required deputies to take an oath of office, and permitted a deputy marshal to be removed only by district court judges. *Id.* § 27, 1 Stat. at 87. Despite the significance of the deputy marshals' authority, however, the statute provided that they be appointed by the marshal himself, not the President, a Court of Law, or the Head of a Department. *See Steele v. United States*, 267 U.S. 505, 508 (1925) ("The deputy marshal is not in the constitutional sense an officer of the United States" despite being "engaged in serving all sorts of writs, and . . . called upon to exercise great responsibility and discretion in the service of some of them, in dealing with the person and property of individuals and in the preservation of their constitutional rights.").

Similarly, the First Congress created various customs officers known as collectors, naval officers, and surveyors, and provided for these Officers to appoint their own deputies who were not themselves considered to be Officers. *See* An Act to Regulate the Collection of the Duties Imposed by Law on the Tonnage of Ships or Vessels, and on Goods, Wares and Merchandises Imported into the United States, ch. 5, § 1, 1 Stat. 29, 29-30 (1789). A 1790 statute provided "[t]hat every collector, naval officer and surveyor, in cases of occasional and necessary absence, or of sickness, and not otherwise, may respectively exercise and perform *their several powers, functions and duties*, by *deputy* duly constituted under their hands and seals respectively, for whom in the execution of the trust they shall respectively be answerable." An Act to Provide More Effectually for the Collection of the Duties Imposed by Law on Goods, Wares and Merchandise Imported into the United States, ch. 35, § 7, 1 Stat. 145, 155 (1790)

(emphasis added). Furthermore, the Act provided that "in the case of the disability or death of a collector, the duties and authorities vested in him shall devolve on his deputy . . . for whose conduct the estate of such disabled or deceased collector shall be liable." *Id.* § 8, 1 Stat. at 155.

Given that deputies were empowered to "exercise and perform" the powers of collectors, naval officers, and surveyors at certain times, it is notable that collectors, naval officers, and surveyors had significant power and responsibilities. For instance, collectors were, among other things, empowered to

> receive the entry of all ships and vessels, and of all the goods, wares and merchandise imported in such ships or vessels, together with the original invoices thereof; to estimate the duties payable thereon, and to endorse the same on each entry; to receive all monies paid for duties, and to take all bonds for securing the payment of duties; [and] to grant all permits for the unlading and delivery of goods, to employ proper persons as weighers, gaugers, measurers and inspectors at the several ports within his district.

Act to Regulate the Collection of the Duties, ch. 5, § 5, 1 Stat. at 36–37. Naval officers were empowered "to receive copies of all manifests, to estimate and record the duties on each entry made with the collector, and to correct any error made therein, before a permit to unlade or deliver shall be granted; [and] to countersign all permits and clearances granted by the collector." *Id.* § 5, 1 Stat. at 37. And surveyors were empowered, among other things, to "superintend and direct all inspectors, weighers, measurers and gaugers within his district, and the employment of the boats which may be provided for securing the collection of the revenue;

to go on board ships or vessels arriving within his district, or to put on board one or more inspectors, . . . and to examine whether the goods imported are conformable to the entries thereof." *Id.*[4]

Even though the deputies to these customs officers were authorized to "exercise and perform [the principal's] several powers, functions and duties" in the principal's sickness, absence, disability, or death, An Act to Provide More Effectually for the Collection of the Duties, ch. 35, § 7, 1 Stat. at 155, they were appointed by their principals, not the President, a Court of Law, or the Head of a Department.

These deputies could be appointed by their principals because, despite their significant responsibilities, they were subordinate to, and acted as agents of, those principals, and those principals were answerable for their deputies' conduct. Indeed, because at the Founding "[a]ctions were personal, against the individual; damages were a normal remedy; and office-holding carried no special immunity from suit," Jerry L. Mashaw, *Recovering American Administrative Law: Federalist Foundations, 1787-1801*, 115 Yale L.J. 1256, 1334 (2006), these early statutes provided that principals "had to assume personal liability for the misdeeds of their deputies," Jennifer J. Mascott, *Who*

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[4] Founding-era evidence suggests that deputies often carried out these significant responsibilities for extended periods. For example, a letter from President Washington explaining why he appointed the deputy collector of the Port of Baltimore, Daniel Delozier, to the role of surveyor for that district explained that Delozier "acted as Deputy to the Collector—and from the ill health of [the incumbent Collector] appears to have done a great pa[r]t of the business of that department, from the time of its organization." Letter from George Washington to Charles Carroll (of Carrollton) (Aug. 25, 1793), https://founders.archives.gov/documents/Washington/05-13-02-0361.

Are "Officers of the United States"?, 70 Stan. L. Rev. 443, 519 (2018); *see, e.g.*, An Act to Establish the Judicial Courts, ch. 20, § 28, 1 Stat. at 87-88 (providing that "defaults or misfeasances" of deputy marshals "shall be adjudged a breach of the condition of the bond given, as before directed, by the marshal who appointed them"). That principals were liable for their deputies' actions reinforces that the First Congress viewed deputies as mere agents of, and subordinate to, their principals, not as Officers in their own right.

2. The same Act that created the collectors, naval officers, and surveyors (and their deputies) also provided for the employment of weighers, gaugers, measurers, and inspectors. Although these individuals, like deputies, had significant statutory responsibilities, they were originally appointed by collectors, not by the President, a Court of Law, or the Head of a Department.[5]

Collectors were authorized "to employ proper persons as weighers, gaugers, measurers and inspectors at the several ports within his district," and surveyors were authorized to "superintend and direct" them. Act to Regulate the Collection of the Duties, ch. 5, § 5, 1 Stat. at 36-37. Though they worked for collectors and surveyors, these non-Officers had significant responsibilities. With regard to inspectors, the Act provided that collectors, naval officers, and surveyors could "put on board [a] ship or vessel one or more inspectors" who (1) ensured that the ship had a permit for all merchandise it was transporting, (2) entered information about the permits in a book, (3) seized suspicious goods after a certain period of time, (4) "compare[d] the account and entries he ha[d] made of the goods unladen from

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[5] Congress subsequently changed their method of appointment to meet the requirements for inferior officers. *See infra* at 16.

such ship or vessel, with the manifest delivered to the collector," and (5) remained with the boat until any inspection was complete. *Id.* § 15, 1 Stat. at 40-41.

Similarly, the statute provided that every "person specially appointed by" collectors, naval officers, and surveyors "shall have full power and authority, to enter any ship or vessel" he believed to contain illicit goods, to "search for, seize, and secure any such goods," and to get "a warrant to enter such house, store, or other place (in the day time only) and there to search for such goods, and if any shall be found, to seize and secure the same for trial." *Id.* § 24, 1 Stat. at 43. The "person[s] specially appointed" to which the statute referred could only have been the weighers, gaugers, measurers, and inspectors that the Act specifically authorized the collectors to hire and surveyors to direct.

Notably, the Fifth Congress changed the appointment procedure for weighers, gaugers, measurers, and inspectors in 1799 to require "the approbation of the principal officer of the treasury department." An Act to Regulate the Collection of Duties on Imports and Tonnage, ch. 22, § 21, 1 Stat. 627, 642 (1799). No evidence from the time, however, suggests that Congress viewed this change as constitutionally required.[6]

3. The view that government employees who had significant duties but acted as agents of, or were subordinate to, Officers were not themselves constitutional "Officers" persisted well after the First Congress, as state supreme court decisions and congressional reports reflect.

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[6] Nearly a half-century later, Attorney General Hugh S. Legaré opined that permanent inspectors must be appointed as inferior officers, *Appointment and Removal of Inspectors of Customs*, 4 Op. Att'y Gen. 162, 163-64 (1843), but neither Congress nor the Attorney General expressed such a view in 1799.

For instance, an oft-cited 1822 opinion by the Maine Supreme Court concluded that an agent for the preservation of timber on the public lands, appointed by the governor, was not a civil Officer such that the state's Incompatibility Clause would prevent a sitting senator or representative from being appointed to the position. *See Opinions of the Justices*, 3 Greenl. (Me.) 481, 481 (1822); *see also Officers of the United States*, 31 Op. O.L.C. at 83-84 (listing many other courts that "treated this early analysis as authoritative"). The court held that an "office" "implies a delegation of a portion of the sovereign power to, and possession of it by the person filling the office." *Opinions of the Justices*, 3 Greenl. at 482. This power is "a legal power, which may be rightfully exercised, and in its effects it *will bind the rights of others*, and be subject to revision and correction only according to the standing laws of the State." *Id.* (emphasis added). Under this definition, the agent for the preservation of timber on public lands was, according to the Court, not an Officer because he was "clothed with no powers, but those of superintending the public lands, and performing certain acts in relation to them *under the discretionary regulations of the governor*." *Id.* at 483 (emphasis added). In other words, although the superintendent of the public lands surely had significant responsibilities, he was not an "Officer" because he was an "agent" of the governor.

Similarly, a House Judiciary Committee report in 1899 concluded that "the member of a commission created by law to investigate and report, but having no legislative, judicial, or executive powers, was not an officer within the meaning of the constitutional inhibition." 1 Asher C. Hinds, *Hinds' Precedents of the House of Representatives* 604 (1907). The Committee rea-

soned that the "mere power to investigate some particular subject and report thereon, or to negotiate a treaty of peace, or on some commercial subject, and report without power to make binding on the Government, does not constitute a person an officer." *Id.* at 607-08. The commission members in question were "*mere agents* appointed by direction of Congress for the purpose of gathering information and making recommendations for its use if the Congress sees fit to avail itself of the labors of the commission." *Id.* at 608 (emphasis added). The Commissioners had "no power to . . . bind the Government" because "[t]heir suggestions and recommendations have no force; they may or may not be adopted" by the Congress. *Id.* at 610. Moreover, the Committee reasoned that the fact "[t]hat the Senate may feel that it ought to ratify or approve the recommendations of such commission can make no difference, [because] the fact remains that their acts are not binding upon anyone or upon any departments of the Government." *Id.* at 611.

4. Consistent with this longstanding approach, Congress has repeatedly over the last century permitted agencies to use ALJs or their equivalents—employees hired based on merit and not pursuant to the Appointments Clause—to help federal agencies develop administrative records and to make initial findings and decisions. Hearing examiners—the contemporary equivalent of today's ALJs—have existed since the turn of the twentieth century. In one early example, Congress permitted the Interstate Commerce Commission to "employ special agents or examiners, who shall have authority under the order of the Commission to inspect and examine any and all accounts, records, and memoranda kept by such carriers." An Act to Amend an Act Entitled "An Act to Regulate Commerce," ch. 3591, § 7, 34 Stat. 584, 594-95 (1906). The

statute did not require that hearing examiners be appointed in the manner prescribed by the Appointments Clause. *Id.*

Even more apposite here, in 1946 Congress passed the Administrative Procedure Act, which maintained and updated the position of hearing examiner. At that time, Congress recognized that "agencies [had] such a volume of business, including cases in which a hearing is required, that the agency heads, the members of boards or commissions, can rarely preside over hearings in which evidence is required." *Ramspeck v. Fed. Trial Exam'rs Conf.*, 345 U.S. 128, 130 (1953). Thus, the APA provided that "[s]ubject to the civil-service and other laws . . . , there shall be appointed by and for each agency as many qualified and competent examiners as may be necessary for proceedings . . . , who shall be assigned to cases in rotation so far as practicable." Pub. L. No. 79-404, § 11, 60 Stat. at 244.

Although the legislative history is ambiguous with respect to how these hearing examiners were to be appointed and whether their appointment outside the process prescribed by the Appointments Clause was seen as raising constitutional concerns,[7] the final text

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[7] *Compare* Administrative Procedure in Government Agencies, S. Doc. No. 77-8, at 47 (1941) (report of a committee appointed by the Attorney General recommending that hearing examiners be appointed by the Office of Federal Administrative Procedure, which would investigate an examiner's "judicial qualifications and capacity" and have "full power to approve and appoint or disapprove and refuse to appoint persons nominated by an agency" without discussing any constitutional concerns), *with* Administrative Procedure Act, Legislative History, S. Doc. No. 79-248, at 42 (1944-46) (Senate report noting that a proposal in which the Office of Administrative Justice appoints hearing examiners may raise constitutional difficulties because it "is a committee and not

of the enacted law did not require that they be appointed in conformity with the Appointments Clause. Rather, the text required that they be "qualified and competent." *Id.* Moreover, they were "given independence and tenure within the existing Civil Service system," and Congress "vest[ed] control of their compensation, promotion and tenure in the Civil Service Commission to a much greater extent than in the case of other federal employees." *Ramspeck*, 345 U.S. at 132; *see id.* at 133 (describing hearing examiners as "classified Civil Service employees").[8] Early regulations implementing the Act provided that "the regulations for appointment to the competitive system . . . shall apply to appointments to hearing examiner positions." 5 C.F.R. § 34.4 (1949); *see, e.g.*, *id.* § 2.109 ("Upon receipt of a request for certification of eligibles, there shall be certified . . . a sufficient number of names to permit the appointing officer to consider three eligibles in connection with each vacancy.").

In 1962, Congress permitted the SEC to use these hearing examiners—who were hired competitively and not pursuant to the Appointments Clause—to assist in completing the Commission's many responsibilities. A proposal submitted by the President to Congress recommended that Congress permit the Commission to delegate some of its responsibilities to employees "for greater flexibility in the handling of the business before the Commission, permitting its disposition at different levels so as better to promote its efficient dispatch." 1961 U.S.C.C.A.N. 1351, 1351. Thus, in An

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a court and hence may not be within the constitutional authorization for appointing powers").

[8] In 1978, the Commission was replaced by the Office of Personnel Management, the Merit Systems Protection Board, and the Federal Labor Relations Authority. *See* Civil Service Reform Act of 1978, Pub. L. No. 95-454, § 201, 92 Stat. 1111.

Act to Authorize the Securities and Exchange Commission to Delegate Certain Functions, Pub. L. No. 87-592, 76 Stat. 394, 394-95 (1962), Congress provided that "the Securities and Exchange Commission, . . . shall have the authority to delegate, by published order or rule, any of its functions to a division of the Commission, an individual Commissioner, a hearing examiner, or an employee or employee board." Congress, however, ensured that the Commission retained the "discretionary right to review the action of any such division of the Commission, individual Commissioner, hearing examiner, employee, or employee board, upon its own initiative or upon petition of a party to or intervenor in such action." *Id.*

In 1978, the term "administrative law judge" was substituted for "hearing examiner." *See* An Act to Amend Title 5, United States Code, Pub. L. No. 95-251, § 2, 92 Stat. 183 (1978). Later that year, Congress specifically codified the requirement that ALJs be required to undergo "competitive examinations" by the Office of Personnel Management before joining the "competitive service." Pub. L. No. 95-454, § 201, 92 Stat. at 1120; *see* 5 C.F.R. § 930.201(d)-(e). Otherwise, the statutory scheme remains the same today.

In short, both the President and Congress agreed that hearing officers and later ALJs should be assigned significant responsibilities to assist the Commission in carrying out its duties. Notwithstanding that, ALJs have never been statutorily required to be appointed by the President, a Court of Law, or the Head of a Department.

* * *

This history demonstrates that, although Congress must wield its power to shape the government in a

manner consistent with the Appointments Clause's requirements, those requirements allow Congress great flexibility in determining how federal employees are hired. From the deputies and customs employees in the First Congress, to hearing officers in the last century, there have been many government employees who exercised significant responsibilities, but were not required to be appointed as constitutional "Officers." Importantly, each of these non-Officers acted as the agent of, or subordinate to, an Officer, and it was the Officer—not the subordinate agent—who was accountable for the agent's actions. As the next section demonstrates, ALJs at the SEC are no different.

III. SEC ADMINISTRATIVE LAW JUDGES ARE NOT CONSTITUTIONAL OFFICERS AND THUS NEED NOT BE APPOINTED IN CONFORMITY WITH THE APPOINTMENTS CLAUSE.

1. ALJs act as agents of, and are subordinate to, the Commissioners of the Securities and Exchange Commission, and their initial decisions never become binding without the Commission's express order. They are therefore not constitutional "Officers of the United States," and need not be appointed by the President, a Court of Law, or the Head of a Department.

As noted earlier, this Court has held that "any appointee exercising significant authority pursuant to the laws of the United States is an 'Officer of the United States.'" *Buckley*, 424 U.S. at 126. In delineating the boundaries of this definition, the Court has reasoned that non-Officers "are lesser functionaries subordinate to officers of the United States" and "subject to the control or direction of any other executive, judicial, or legislative authority." *Id.* at 126 n.162; *see also Tucker v. Comm'r*, 676 F.3d 1129, 1134 (D.C. Cir.

2012) (employees are not "Officers" where they are "subject to consultation requirements, to guidelines, and to supervision"). Other authorities have similarly reasoned that "Officers of the United States" are only those who have "power lawfully conferred by the government to *bind third parties*, or the government itself, for the public benefit," *Officers of the United States*, 31 Op. O.L.C. at 87; *see* 1 *Hinds' Precedents* at 610 (non-Officers may not "bind the Government").

ALJs are lesser functionaries "subject to the control" of the SEC and do not have the power in their own right to bind third parties or the government. Though ALJs conduct hearings, their "initial decisions" are not final, let alone binding. *See* 17 C.F.R. § 201.360(a)(1) & (d). Once the ALJ issues an initial decision, "a party or an aggrieved person [may] timely file[] a petition for review or a motion to correct a manifest error of fact in the initial decision," *id.* § 201.360(d)(1), which the Commission always grants, *see* App. 89a. The Commission may also "on its own initiative order[] review of a decision." 17 C.F.R. § 201.360(d)(1). Even when an aggrieved party or person fails to file a timely petition for review and the Commission does not order a review on its own initiative, the Commission must "order that the decision has become final as to that party," and "[t]he decision becomes final" only "upon issuance of the order" by the Commission. *Id.* § 201.360(d)(2). Put differently, "ALJs' initial decisions . . . do not become the final and effective decision of the agency without affirmative action on [the Commission's] part—specifically, [its] issuance of a finality order."

App. 90a n.109; *see id.* at 90a ("no initial decision becomes final simply 'on the lapse of time' by operation of law").[9]

Moreover, the Commission reviews the initial decisions of ALJs *de novo*. *Id.* at 91a. The Commission "may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part, an initial decision by a hearing officer and may make any findings or conclusions that in its judgment are proper and on the basis of the record." 17 C.F.R. § 201.411(a). It also may, "[u]pon its own motion or the motion of a party, . . . allow the submission of additional evidence." *Id.* § 201.452. In short, "although ALJs may play a significant role in helping to shape the administrative record initially, it is the Commission that ultimately controls the record for review and decides what is in the record." App. 91a.

Finally, "[b]ecause the Commission is not bound in any way by its ALJ's decisions, . . . the blame for its

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[9] Petitioners and the United States argue that "[i]n about 90% of cases . . . the ALJ's initial decision 'become[s] final without plenary agency review,'" Pet'rs Br. 32 (quoting *Bandimere*, 844 F.3d at 1180 n.25); *see* U.S. Br. 22, but a recent study by a current SEC Commissioner examined all SEC ALJ decisions from 2014 to 2015 and found that "[f]ully 80 percent of the ALJ decisions during that period were *default* decisions" in which the respondent did not appear. Robert J. Jackson, Jr., *Fact and Fiction: The SEC's Oversight of Administrative Law Judges*, The CLS Blue (Mar. 9, 2018), http://clsbluesky.law.columbia.edu/2018/03/09/fact-and-fiction-the-secs-oversight-of-administrative-law-judges/. "In the rest of the cases, the respondent appeared," but "chose not to ask the commission to review the case." *Id.* Indeed, so far as that Commissioner is aware, "the only proceeding . . . during this time period where review of an ALJ's decision was timely sought and the commission refused review was one in which the SEC's own enforcement division made the request." *Id.* (emphasis omitted).

unpopular decisions will fall squarely on the commissioners and, in turn, the president who appointed them." *Bandimere*, 844 F.3d at 1198 (McKay, J., dissenting). The relevant statute permits "[a]ny person aggrieved by *an order of the Commission* [to] obtain a review of such order in the court[s] of appeals of the United States." 15 U.S.C. § 77i(a). In other words, in the same way that marshals and customs officers created by the First Congress were liable for their deputies' misdeeds, only orders of the Commission—the only orders that have any binding effect—may form the basis of a challenge in an Article III court.

As this Court has suggested, then, ALJs at the SEC "possess purely recommendatory powers." *Free Enter. Fund*, 561 U.S. at 507 n.10; *cf. Attorney General's Manual* at 83 (agencies are "in no way bound by the decision" of ALJs and "retain[] complete freedom of decision—as though [they] had heard the evidence [themselves]"). For that reason, they are quintessentially "lesser functionaries subordinate to officers of the United States," *Buckley*, 424 U.S. at 126 n.162—namely, the Commissioners of the SEC. Moreover, because an initial ALJ decision does not become final without the *de novo* review of and order by the Commission, ALJs do not themselves have the power "to bind third parties, or the government itself, for the public benefit," *Officers of the United States*, 31 Op. O.L.C. at 87.

Petitioners' theory rests heavily on this Court's decision in *Freytag*, but that case is not to the contrary. There, the Court held that special trial judges of the Tax Court were "inferior Officers" in part because of "the significance of the duties and discretion that special trial judges possess." 501 U.S. at 881. But part of the reason special trial judges enjoy significant discretion is because the Tax Court is required to defer to a

special trial judge's fact and credibility findings unless they are "clearly erroneous." *Landry v. Fed. Deposit Ins. Corp.*, 204 F.3d 1125, 1133 (D.C. Cir. 2000); *see* Tax Ct. R. 183(d) ("the findings of fact recommended by the Special Trial Judge *shall* be presumed to be correct" (emphasis added)). At the SEC, by contrast, the Commission reviews all of an ALJ's factual findings *de novo*. *See supra* at 24. Moreover, it was important to the *Freytag* Court that in the case of declaratory judgment proceedings and limited-amount tax cases, special trial judges "render[ed] the decisions of the Tax Court" with no subsequent order or sign off from a higher official. *Freytag*, 501 U.S. at 882. Thus, the special trial judges exercised precisely the type of "independent authority," *id.*, that ALJs at the SEC do not have.

Notably, the facts of *Freytag* contrast starkly with the facts here. In *Freytag*, although the special trial judge presided over a two-year trial, including 14 weeks of complex financial testimony and 3,000 exhibits, the special trial judge's decision was filed as the Tax Court's decision on the same day the Tax Court received the trial judge's report, suggesting essentially no review or oversight of special trial judges whatsoever. *See Bandimere*, 844 F.3d at 1195 (McKay, J., dissenting). By contrast, here, the ALJ issued an initial decision, the Commission remanded the case for further findings of fact, the ALJ issued a revised initial decision, the Commission granted review, and on an independent review of the record and in a detailed opinion the Commission found that Petitioners committed anti-fraud violations. App. 8a-9a.

Petitioners also attempt to analogize ALJs to court commissioners, the predecessors of magistrate judges, whom the Court held were inferior Officers in *Go-Bart Importing Company v. United States*, 282 U.S. 344,

352 (1931). *See* Pet'rs Br. 20. But court commissioners performed a variety of significant duties that could bind third parties. They were empowered under federal statute, among other things, "to arrest and imprison, or bail, for trial," "to issue warrants for and examine persons charged with being fugitives from justice," "to hold to security of the peace and for good behavior," "to issue search warrants," "to take bail and affidavits in civil causes," "to discharge poor convicts imprisoned for non-payment of fines," "to institute prosecutions under laws relating to the elective franchise and civil rights and to appoint persons to execute warrants thereunder," and "to enforce arbitration awards of foreign consuls in disputes between captains and crews of foreign vessels." *Go-Bart*, 282 U.S. at 353 n.2 (citations omitted). ALJs do not come close to having this panoply of significant powers; to the contrary, as previously explained, ALJ initial decisions have no power to bind third parties in their own right.

In short, although ALJs certainly have been granted important responsibilities by the Commission to aid the Commission's work, they do not "exercis[e] significant authority pursuant to the laws of the United States" for purposes of Article II. Thus, they may be hired through a merit-based system, rather than in the manner prescribed by the Appointments Clause.

2. Were this Court to conclude otherwise, the disruption to the operations of the federal government could be substantial. This Court has repeatedly insisted that the vast majority of civil servants in the federal government do not qualify as constitutional "Officers." *See supra* at 9. That is because, though many civil servants have significant responsibilities and exercise substantial discretion on a day-to-day ba-

sis, they are agents of, or otherwise subordinate to, Officers and therefore do not "exercis[e] significant authority" for Appointments Clause purposes. "Our government in fact depends on such delegation of responsibility, and it does not offend the Appointments Clause so long as the duly appointed official has final authority over the implementation of the governmental action." *Andrade*, 824 F.2d at 1257.

Petitioners and their *amici*, however, would have this Court adopt a much broader test, suggesting that any civil servant who has "substantive and procedural powers that require the exercise of broad discretion" is an "Officer" and must be appointed in conformity with the Appointments Clause. Pet'rs Br. 21; *see* Br. of *Amici Curiae* Scholars of Corpus Linguistics 19 (the term "Officer of the United States" "applie[s] broadly to all government employees—'civil and military'—exercising any non-trivial federal authority"); Br. of Professor Jennifer L. Mascott as *Amicus Curiae* in Supp. of Pet'rs 2 ("Officer" encompasses "every federal civil official with ongoing responsibility to carry out a statutory duty"). These definitions, which focus on the day-to-day discretion of government workers rather than whether or not they independently bind third parties or act as agents of, or subordinate to, other Officers, have the potential to sweep in all sorts of civil servants.[10]

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[10] Notably, Petitioners' theory would invalidate appointments allowed by the First Congress. For instance, under Petitioners' theory, deputy marshals would have been required to be appointed as Officers because they carried out the same significant responsibilities that marshals did. Similarly, inspectors were delegated significant duties by the First Congress, and under Petitioners' theory, those job duties alone would make them constitutional "Officers."

For one thing, though only five ALJs work at the SEC, there are thousands of other ALJs working throughout the federal government. *See Free Enter. Fund*, 561 U.S. at 542 (Breyer, J., dissenting); *see also* Administrative Law Judges, Office of Pers. Mgmt., https://www.opm.gov/services-for-agencies/administrative-law-judges/#url=ALJs-by-Agency (last visited Mar. 28, 2018). The Social Security Administration alone employs 1,655 ALJs, while dozens more ALJs assist agencies as varied as the Federal Mine Safety and Health Review Commission, the Department of Labor, and the Office of Medicare Hearings and Appeals at the Department of Health and Human Services. *Id.* Many of these ALJs have responsibilities similar to those of SEC ALJs. *See Bandimere*, 844 F.3d at 1199 (McKay, J., dissenting). In addition, more than 3,000 administrative judges, who lack the independence of ALJs but perform similar functions, also populate the Executive Branch. *See generally* Kent Barnett, *Against Administrative Judges*, 49 U.C. Davis L. Rev. 1643, 1652-62 (2016).

If Petitioners' theory is correct, "every losing party before an ALJ [might] now have grounds to appeal on the basis that the decision entered against him is unconstitutional[.]" *Free Enter. Fund*, 561 U.S. at 543 (Breyer, J., dissenting). Indeed, "Appointment Clause problems may exist even in . . . agencies where the agency head does select the ALJs, given [the Office of Personnel Management's] role in limiting the pool of ALJ candidates and the fact that some agency heads may not qualify as department heads for constitutional purposes because their agencies are nested within bigger administrative entities." Gillian E. Metzger, *Foreword: 1930s Redux: The Administrative State Under Siege*, 131 Harv. L. Rev. 1, 20 n.99 (2017).

Though there may be ways to distinguish among different types of ALJs or other administrative judges, a ruling for Petitioners would at least open the door to constitutional challenges from nearly everyone who is regulated by an administrative agency, swamping courts and destabilizing the government's ability to function.

Moreover, Petitioners' definition of "Officer" would seemingly include other federal employees who have never been considered Officers. For example, there are 3,684 career employees in the Senior Executive Service who have significant responsibilities, but are subordinate to Officers. *See* S. Comm. on Homeland Sec. and Gov't Affairs, 114th. Cong., *Policy and Supporting Positions* 216 (Comm. Print 2016), http://www.fdsys.gov; *see id.* at 217-18 (describing the merit-based hiring of these career employees). If these career positions were considered Offices under the Appointments Clause, the individuals filling those positions would have to be appointed by Presidential nomination and Senate confirmation, until and unless Congress said otherwise. This would be a revolutionary change in how the government functions.

On top of this, Petitioners' theory threatens to eliminate the dual layer of removal protection afforded to ALJs and other civil servants who have significant responsibilities because this Court has held that "dual for-cause limitations on the removal" of some inferior Officers violates the constitutional separation of powers. *Free Enter. Fund*, 561 U.S. at 492. Under federal law, ALJs may be removed by the Merit Systems Protection Board only for good cause, *see* 5 U.S.C. § 7521(a), (b), and members of the Merit Systems Protection Board may be removed "only for inefficiency, neglect of duty, or malfeasance in office," *id.* § 1202(d). This, of course, is a common way to structure how civil

servants in independent agencies can be removed. *See Free Enter. Fund*, 561 U.S. at 540-52 (Breyer, J., dissenting) (listing examples). But Petitioners' theory throws into doubt the constitutionality of these long-standing removal provisions and contravenes this Court's warning not to "cast doubt on the use of what is colloquially known as the civil service system within independent agencies," *id.* at 507 (majority opinion).[11]

In short, on top of rowing against centuries of practice in which Congress has chosen how government employees who are agents of, or subordinate to, Officers should be hired, Petitioners' theory threatens to destabilize the modern federal government and throw into doubt the constitutionality of how thousands of civil servants who work in every corner of the federal government are hired. Given that dramatically expanding the number of appointments that must be made in conformity with the Appointments Clause will significantly undermine the federal government's ability to function, efforts to minimize that disruption will

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[11] The United States argues that this Court should decide this removal question now, even though the Court was specifically asked to grant *certiorari* on it and declined to do so. Contrary to the views of the United States, that question is not "fairly encompassed" in the question this Court did grant, U.S. Br. 39 n.7, because dual for-cause limitations on removal may be permissible for some inferior Officers, *see Free Enter. Fund*, 561 U.S. at 507 n.10. Put differently, whether ALJs are "Officers" is a separate question from whether their removal protections "interfere impermissibly with [the President's] constitutional obligation to ensure the faithful execution of the laws," *Morrison v. Olson*, 487 U.S. 654, 692-93 (1988), and this Court should not decide that question without full briefing on the meaning of "good cause," whether "good cause" limitations on SEC ALJs "interfere impermissibly with [the President's]" Take Care obligations, and other related questions.

inevitably lead to *pro forma* appointments, thereby undermining the accountability goals that animate the Clause.

Rather than go down that path, this Court should reaffirm that "lesser functionaries subordinate to officers of the United States" and "subject to the control or direction of any other executive, judicial, or legislative authority" are not "Officers of the United States," *Buckley*, 424 U.S. at 126 n.162.

CONCLUSION

For the foregoing reasons, the judgment of the U.S. Court of Appeals for the District of Columbia Circuit should be affirmed.

Respectfully submitted,

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No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, *et al.*,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DC CIRCUIT

BRIEF FOR CORNELL SECURITIES LAW CLINIC AS *AMICUS CURIAE* IN SUPPORT OF THE JUDGMENT BELOW

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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INTEREST OF THE *AMICUS CURIAE*

The Cornell Securities Law Clinic (the "Clinic") is approved to operate as a law school clinic by the New York State Appellate Division, Third Department, and is a curricular offering of Cornell Law School. Cornell Law School is part of Cornell University, which is a private and statutory not-for-profit educational corporation registered in the State of New York. The Clinic offers second- and third-year law students an opportunity, among other things, to provide supervised representation to small investors, primarily in upstate New York.[1] The Clinic has a strong interest in protecting the rights of investors.

The present case involves, among other things, determining whether the decisions of the administrative law judges ("ALJs") of the Securities and Exchange Commission ("SEC" or the "Commission") were unconstitutionally rendered and defining who is an Officer under the Appointments Clause. The issues raised in this case are directly relevant to the Clinic's mission and work.

CONSTITUTIONAL PROVISION AT ISSUE

Article II, Section 2, Clause 2 of the U.S. Constitution provides:

> [The president] shall have Power, by and with the Advice and Consent of the Senate, to make

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1. No counsel for any party authored this brief in whole or in part, and no person, other than the Clinic, made a monetary contribution intended to fund the preparation or submission of this brief. All parties lodged a blanket consent with the Clerk.

> Treaties, provide two thirds of the Senators present concur; and he shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law; but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

SUMMARY OF THE ARGUMENT

The Court should affirm the decision of the U.S. Court of Appeals for the District of Columbia Circuit.[2]

I. SEC ALJs are not Officers for the purposes of the Appointments Clause because they do not have final decision-making power in any circumstance. Contrary to Petitioners' assertions, this Court's precedent shows that final decision-making authority is a necessary aspect of every Officer of the United States. This Court has previously found individuals to be Officers when they

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2. The amicus curiae respectfully adopts, in relevant part, the facts as set forth in the decision below, *Raymond J. Lucia Co. v. SEC*, 832 F.3d 277, 281–83 (D.C. Cir. 2016). Citations to "Pet. Br." refer to Petitioners' brief filed in this case. As the Respondent SEC filed a brief in support of Petitioners, we include citations to the SEC Brief, but only refer to the SEC's arguments when they differ from Petitioners' arguments. We cite to the SEC's brief as "SEC Br."

act with final decision-making power in at least some circumstances. SEC ALJs, however, do not issue a final decision in *any* circumstance. Every action an SEC ALJs takes is subject to review by the Commission. Thus, SEC ALJs merely assist the Commission in exercising its enforcement power and are therefore not Officers under the Appointments Clause.

II. The legislative history and the statutory scheme of the Administrative Procedure Act (APA), 5 U.S.C. § 500 *et seq.*, support the finding that SEC ALJs are not Officers of the United States.

A. The APA is where Congress devised the office of the Administrative Law Judges for all agencies. Petitioners point out that Congress referred to hearing examiners, the predecessors to ALJs, as officers numerous times throughout the APA. Petitioners fail to mention, however, that Congress did not refer to examiners as officers a single time in § 11 of the APA. This is significant because § 11 specifically deals with the appointment and removal of "Examiners"—i.e., ALJs. This shows that in devising the office of the ALJ, Congress did not intend the ALJs to be Officers of the United States.

B. Moreover, had Congress intended for SEC ALJs to be Officers of the United States, it would have included express language to that effect—either by including that phrase or by mentioning, or otherwise clearly implicating, the Appointments Clause. This Court has recognized that where Congress knows how to attach particular meaning to a statutory scheme, its failure to do so is reasonably construed as purposeful. Congress knows how to create an office that would be appointed pursuant to the Appointments Clause. It did not do so here.

C. Finally, to the extent the term "officers" in the APA is ambiguous—i.e., there are two possible interpretations: Officer of the United States or employee—that ambiguity should be resolved to avoid constitutional questions.

III. The Court should reject Petitioners' position and hold that SEC ALJs are not Officers of United States to avoid two serious legal ramifications.

A. First, Petitioners' position would render a portion of the Appointments Clause superfluous. The Appointments Clause applies to any office that is "established by Law." SEC ALJs, however, are not directly established by any statute. Rather, Congress passed a statute *authorizing* but not mandating the Commission to appoint ALJs. A separate rule of the Commission creates the office of the SEC ALJ. Thus, Petitioners interpret "established by Law" as covering any office that is authorized by any legal authority, be it a statute, rule, etc. Yet this interpretation would mean that the provision "established by Law" has no limiting effect, because every government employee holds an office that is created by a statute, rule, executive action, or other legal authority. To give effect to the established by Law provision, the Court should limit its application only to offices directly created by statute.

B. Second, Petitioners' definition for who is an Officer of the United States is so overbroad it would produce an absurd result, for example, of applying constitutional requirements to members of Self-Regulatory Organizations (SROs). As explained below, Petitioners' definition consists of two prongs: first, that the office is established by some legal authority; and second, that the officials holding that office exercise significant government

authority. FINRA disciplinary hearing officers, for example, would satisfy the first prong despite the fact that their office is not directly created by statute. FINRA disciplinary hearing officers also would satisfy the second prong because they, like ALJs, conduct hearings, rule on admissibility of evidence, and issue initial decisions. Thus, under Petitioners' definition, FINRA disciplinary hearing officers would be subject to the Appointments Clause. This conclusion, however, is contrary to law and public policy. This Court previously recognized that SROs are non-government entities and do not become a part of the government absent Congressional control over the SRO board.

IV. If this Court nonetheless determines that SEC ALJs are Officers of the United States, then remand for a new hearing is the appropriate remedy. Although Petitioners argue for dismissal, there is no legal grounds for this remedy. Even if Petitioners received unconstitutional process, the outcome may have been valid.

ARGUMENT

The D.C. Circuit correctly concluded that SEC ALJs are not Officers of the United States because they do not have the authority to enter a final decision on any matter. *See Lucia*, 832 F.3d at 283–89. This holding is consistent with this Court's precedent and Congressional intent. Petitioners' position, on the other hand, that: (i) "established by Law" should cover offices created by agency rules, rather than be limited to those expressly created by statute; and, (ii) the exercise of "significant authority" should not require final decision-making authority, is untenable. *See* Pet. Br. at 20–26; SEC Br. at 14

(focusing on significant authority prong alone). Petitioners' position renders the "established by Law" provision of the Appointments clause superfluous and potentially applies to FINRA hearing officers. Accordingly, the Court should affirm the decision below.

I. SEC ALJS ARE NOT OFFICERS UNDER THE APPOINTMENTS CLAUSE BECAUSE THEY DO NOT HAVE FINAL DECISION-MAKING AUTHORITY.

Petitioners assert that SEC ALJ's are "established by Law" and "exercise authority . . . deemed sufficiently significant" to conclude that SEC ALJs are Officers under the Appointments Clause. *See* Pet. Br. at 20; SEC Br. at 25–32. According to Petitioners, "SEC ALJs unquestionably exercise significant authority pursuant to the laws of the United States," because they: "amend[] charging documents"; "enter[] orders of default"; "consolidat[e] proceedings"; "[a]dminister oaths and affirmations"; "[i]ssue subpoenas"; issue an initial decision; and otherwise regulate the course of the administrative proceeding. Pet. Br. at 21–22; SEC Br. at 20. Petitioners then assert that under this Court's holdings in *Buckley v. Valeo*, 424 U.S. 1 (1976), *Freytag v. Commissioner*, 501 U.S. 868 (1991), and *Edmond v. United States*, 520 U.S. 651 (1997) any individual who possesses an office established by Law and exercises significant government authority is an Officer for the purposes of the Appointments Clause. Pet. Br. at 16–20; SEC Br. at 23–24. Petitioners thus conclude that SEC ALJs are Officers of the United States. Pet. Br. at 26.

Petitioners misread this Court's precedent. In determining whether a federal employee was an Officer,

this Court has always focused on final decision-making authority. Thus, while it is true that the Commission has granted ALJs with authority over powers such as taking testimony and ruling on the admissibility of evidence, SEC ALJs do not have final decision-making authority, and therefore do not exercise "significant authority." *See* 15 U.S.C. § 78d-1 (2012). Hence, this Court should affirm the decision below and endorse the D.C. Circuit's analysis of whether ALJs are Officers under the Appointments Clause.

The Appointments Clause requires that only duly appointed "Officers of the United States" exercise such powers that represent "the performance of significant governmental duty exercised pursuant to public law." *Buckley*, 424 U.S. at 140–41. In *Buckley*, the Court considered whether the appointment of the Federal Election Commission ("FEC") was unconstitutional. In analyzing the extent of the FEC's powers, the Court focused on whether the FEC merely aided Congress in fact-finding, in which case it was constitutional, *see id.* at 137, or whether it exercised independent, executive power, *see id.* at 138. The Court explained that "investigative and informative powers" do not constitute significant authority, while "interpretive and rulemaking powers, such as the power to issue regulations or make determinations without supervision," do constitute significant authority. *Id.* at 137–142. The FEC, however, was charged with fact-finding, rulemaking, and enforcement functions. *Id.* The Court emphasized that the FEC performed these functions "free from day-to-day supervision." *Id.* at 140–41. Because the FEC exercised authority independent of Congress, the Court could not conclude that they merely assisted Congress. *Id.* at 141. Accordingly, the FEC commissioners were deemed Officers of the United States. *Id.*

Similarly, the special trial judges in *Freytag* exercised significant authority because of the important duties they were assigned and because they had final decision-making authority. *See* 501 U.S. at 882. In *Freytag*, the special trial judges of the Tax Court were authorized to take testimony, conduct trials, rule on the admissibility of evidence, and enforce compliance with discovery orders. *Id.* at 881–82. In holding that the special trial judges were Officers, the Court focused on the fact that the judges had authority to issue final decisions in at least some cases. *Id.* at 882. That is, under §§ 744A(b)(1), (2), and (3) of the Tax Reform Act of 1969, the Chief Judge had authority to allow special trial judges to render final decisions of the Tax Court. *Id.* Much like the FEC in *Buckley*, the Tax Court judges exercised independent authority "free from day-to-day supervision" in at least some instances. *Compare Buckley*, 424 U.S. at 137–42, *with Freytag*, 501 U.S. at 881–82. For this reason, this Court correctly concluded that the Tax Court judges were Officers because they did not exist merely to assist another office; they were final decision-makers.

Finally, *Edmond* involved intermediate appellate military judges. 520 U.S. at 662. These judges were authorized to "independently 'weight the evidence, judge the credibility of witnesses, and determine controverted questions of fact.'" *Id.* (quoting 10 U.S.C. § 866(c)). As Petitioners correctly observe, however, the judges "could enter 'a final decision on behalf of the United States' when 'permitted to do so by other Executive Officers.'" Pet. Br. at 19 (quoting *Edmond*, 520 U.S. at 665). Thus, even the judges in *Edmond* had final decision-making power.

In contrast, SEC ALJs are not Officers under the Appointments Clause because, while they do have

significant powers overseeing administrative hearings, they do not have final decision-making authority. Similar to the judges in *Freytag* and *Edmond*, the SEC ALJs exercise authority over several matters during administrative hearings—such as entering orders of default, issuing subpoenas, taking testimony, and ruling of the admissibility of evidence. *See* Pet. Br. at 21–23; SEC Br. at 16. Unlike the special trial judges, however, no action of the SEC ALJ is independently final until the Commission issues the "finality order." *Lucia*, 832 F.3d at 286. Under 15 U.S.C. § 78d-1(b), "the Commission shall retain a discretionary right to review the action of any . . . administrative law judge . . . upon its own initiative or upon petition of a party." Therefore, this case is unlike *Freytag* or *Edmond* because the ALJs exist to assist the Commission in its decision-making; the ALJs are not independent actors and the Commission retains a right to review all decisions by SEC ALJs. 15 U.S.C. § 78d-1(b). *Compare with Edmond*, 520 U.S. at 665, *Freytag*, 501 U.S. at 882, *and Buckley*, 424 U.S. at 137–42.

In this particular case, the Commission did not blindly accept the ALJ's determination but chose to review the decision of the ALJ because the findings of the case were "a matter of considerable importance" to the Commission. *See* Pet. Br. at 24. This shows that the Commission is the one wielding significant government power to enforce the securities laws, not the ALJ. The ALJ merely assists the Commission. Thus, while it is true that SEC ALJs have considerable authority in taking testimony and ruling on the admissibility of evidence, the fact that they never have final decision-making authority is clearly distinguishable from the judges in *Edmond* and *Freytag*. Accordingly, SEC ALJs do not exercise "significant authority," and

therefore should not be considered Officers under the Appointments Clause.

For this reason, the Court should reject Petitioners' position and adopt the D.C. Circuit's well-reasoned approach to determining when a government official truly wields significant government authority. According to the D.C. Circuit, in order to qualify as such, ALJs must perform important functions that exercise significant discretion and have final decision-making authority. *Landry v. Fed. Deposit Ins. Corp.*, 204 F.3d 1125, 1133–34 (D.C. Cir. 2000).

In *Landry*, the D.C. Circuit acknowledged the similarities between the special trial judges of *Freytag* and ALJs. *Id.* at 1133–1134. Nonetheless, the D.C. Circuit concluded that ALJ's authority was not as broad as the special trial judges' authority because the ALJs can never render final decisions. *Id.* at 1134. ALJs can only file a "recommended decision, recommended findings of fact, recommended conclusions of law, and a proposed order." *Id.* at 1133. The D.C. Circuit remarked that if recommendatory powers of the special trial judges in *Freytag* were sufficient to hold the judges as Officers, then this Court would not have focused on the judges' final decision-making power. *Id.*

Then in *Tucker v. Commissioner*, 676 F.3d 1129 (D.C. Cir. 2012), the D.C. Circuit identified three "main criteria" for determining when an office is vested with "significant authority": (1) power over "significant" or important matters; (2) "discretion"; and (3) final decision-making authority. *Id.* at 1133. First, "significant important matters" is a fact-intensive analysis that requires the

court to determine whether the matters are important or meaningful in nature. *Id.* Second, an office is vested with discretion when the tasks of its holder are more than ministerial. *See Freytag*, 501 U.S. at 881. An office will lack discretion where the office-holder has no choice but to act in a certain way. *See Tucker*, 676 F.3d at 1134. Third, an office holder has final decision-making authority when the office holder can enter a decision on behalf of an agency that is final in at least some circumstances. *Tucker*, 676 F.3d at 1133–134.

The D.C. Circuit's test is a logical interpretation and application of the decision in *Freytag*. Applying its test to the facts of this case, SEC ALJs are not Officers of the United States because they lack final decision-making power. Accordingly, this Court should uphold the decision below.

II. CONGRESS DID NOT INTEND TO ESTABLISH ADMINISTRATIVE LAW JUDGES AS OFFICERS OF THE UNITED STATES.

In arguing that Congress intended for SEC ALJs to be Officers of the United States subject to the Appointments Clause, Petitioners assert that the APA "specifically recognize[d] ALJs—or, as they were known then, 'hearing examiners'—as 'officers'" because "[t]he APA, as enacted, [] referred to hearing examiners as 'subordinate officers' or 'officers' *nine* times." Pet. Br. at 36. In doing so however, Petitioners neglect to mention that under § 11 of the APA, which is titled "Examiners" and deals specifically with their appointment and removal, hearing examiners are exclusively referred to as just that—there is no reference to, or mention of, "officers"

whatsoever. Moreover, Petitioners gloss over the fact that while Congress could have included express language clearly indicating that references to "officers" within other provisions of the APA are in fact references to Officers of the United States subject to the Appointments Clause, it did not do so.

Petitioners also argue that, because SEC ALJs "ultimately exercise *executive* power" and are not wholly independent tribunals, they must necessarily be executive Officers. Pet. Br. at 35. This argument not only disregards the statutory safeguards Congress included under § 11 of the APA in order to provide hearing examiners with some degree of adjudicatory independence (and by extension, insulation from political control), but also incorrectly circumvents the emphasis *Freytag* placed on the degree of governmental authority exercised rather than the mere exercise of it. *See Freytag*, 501 U.S. at 881–82.

Finally, under a longstanding principle of statutory construction, where there are competing interpretations of ambiguous statutory language, this Court should resolve that ambiguity in a manner that avoids constitutional issues if such a construction is reasonable and not plainly contrary to congressional intent. *Concrete Pipe & Prod. of Cal., Inc. v. Constr. Laborers Pension Tr. for S. Cal.*, 508 U.S. 602, 628–29 (1993) (quoting *Edward J. DeBartolo Corp. v. Fla. Gulf Coast Bldg. & Constr. Trades Council*, 485 U.S. 568, 575 (1988)).

A. Congress Did Not Refer to ALJs as Officers a Single Time in § 11 of the APA, Which Provided for the Appointment of Examiners to Preside Over Administrative Proceedings.

Petitioners emphasize that the text of "[t]he APA, as enacted, [] referred to hearing examiners as 'subordinate officers' or 'officers' *nine* times." Pet. Br. at 36. They argue that the sole reasonable interpretation of these references is to read the APA as having established hearing examiners (the predecessors to ALJs) as Officers of the United States. *Id.* In doing so, Petitioners rely on this Court's holding in *United States v. Germaine*, 99 U.S. 508 (1879), for the proposition that "the Appointments Clause is triggered when Congress denominates an official an 'officer.'" Pet. Br. at 35. The *Germaine* Court held that if Congress, through statutory language, meant to refer to something other than "officers as defined by the Constitution, words to that effect would be used, as servant, agent, person in the service or employment of the government." *Germaine*, 99 U.S. at 510.

Petitioners neglect to mention, however, that while it is true that the text of the APA includes a few references to "officers" within some of its provisions, there is no mention of, or reference to, the term within § 11—which is titled "Examiners" and deals specifically with their appointment and removal. Administrative Procedure Act, Pub. L. No. 79-404, § 11, 60 Stat. 237, 244 (1946) (codified at 5 U.S.C. §§ 551–59 (2012)). Section 11, being the section of the APA directly concerned with the placement of hearing examiners within the administrative system, would appear to be the most insightful as to whether Congress intended to establish them as Officers of the United

States rather than agency employees. Moreover, neither the House nor the Senate, in the reports issued by their respective Committees on the Judiciary recommending that the APA be passed, provide any indication that hearing examiners should be considered Officers of the United States subject to the Appointments Clause. *See generally* H.R. Rep. No. 79-1980 (1946); *id.* at 26–31, 34–37, 46 (for the explanatory sections most relevant to hearing examiners); *see generally* S. Rep. No. 79-752 (1945); *id.* at 16–18, 20–23, 46 (for the explanatory sections most relevant to hearing examiners). In fact, there is no mention of, or reference to, the Appointments Clause at all. H.R. Rep. No. 79-1980; S. Rep. No. 79-752. These omissions are particularly significant because each committee dedicated a substantial portion of their respective reports to providing a detailed explanation for each of the APA's statutory provisions. H.R. Rep. No. 79-1980; S. Rep. No. 79-752.

Congress's silence, in omitting any mention of, or reference to, "officers" from the statutory language of § 11, strongly evidences its intent to establish hearing examiners as agency employees rather than executive Officers. While it is true that, as Petitioners point out, Congress included generic references to "officers" when discussing hearing examiners within other provisions of the APA, § 11 stands out as being the critical missing piece to Petitioner's constitutional puzzle. Applying this Court's holding in *Germaine*, Congress did in fact use words other than "officer" within § 11 to describe agency officials presiding over adversarial agency adjudications—and so it must not have intended for these examiners to be considered Officers of the United States subject to the Appointments Clause. Additionally, the absence of

any express indication that hearing examiners should be considered Officers of the United States subject to the Appointments Clause from the extensive, explanatory portions of both the House and Senate judicial committee reports provides further evidence of Congress's intent to establish them as agency employees, not as Officers of the United States.

B. If Congress Wanted to Establish Examiners as Officers of the United States, It Would Have Included Express Language to that Effect.

Petitioners also fail to provide any argument for why Congress decided not to include, anywhere in the APA, any express language clearly indicating that references to "officers" outside of § 11 are in fact references to Officers of the United States subject to the Appointments Clause. This Court has recognized that where Congress knows how to attach particular meaning to a statutory scheme, its failure to do so is reasonably construed as purposeful. *See Cnt. Bank of Denver v. First Interstate Bank*, 511 U.S. 164, 176–77 (1994) (where the Court rejected respondents' argument that the "[i]nclusion of those who act 'indirectly' suggests a legislative purpose fully consistent with the prohibition of aiding and abetting" because if "Congress intended to impose aiding and abetting liability, . . . it would have used the words 'aid' and 'abet' in the statutory text.").

Here, the APA, like the statute at issue in *Central Bank of Denver*, includes ordinary language that could be afforded extraordinary effect. *Id.* However, applying the reasoning of *Central Bank of Denver* leads to the opposite conclusion because Congress knows how to refer

to "Officers of the United States" unambiguously and in such capacity as to invoke the Appointments Clause, but did not do so anywhere within the APA. For example, in *Germaine*—Petitioners' principal case for interpreting general references to "officers" within the APA as actually referring to "Officers of the United States"—the defendant was indicted under a statute in which Congress did exactly that. 99 U.S. at 509 (where defendant was indicted under § 12 of the so-called Crimes Act of 1825, 4 Stat. 118, which reads, "'Every *officer of the United States* who is guilty of extortion under color of his office shall be punished by a fine of not more than $500, or by imprisonment not more than one year, according to the aggravation of his offence.'" (emphasis added)).

Considering the lengthy legislative history of the APA, along with the substantial attention it received from both the Executive and the general public, it seems unlikely that Congress would tiptoe around such a critical issue—particularly when it has had no difficulty clearly and unambiguously identifying Officers of the United States subject to the Appointments Clause when it so desires. *See id.*; *see generally* President's Comm. on Admin. Mgmt., *Administrative Management in the Government of the United States* (1937). In other words, "Congress . . . does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions—it does not . . . hide elephants in mouseholes." *Whitman v. Am. Trucking Ass'ns.*, 531 U.S. 457, 468 (2001).

C. Given a Reasonable Option, Any Statutory Ambiguity Within the APA Should be Resolved in a Manner That Avoids Constitutional Issues.

Collectively, the lack of any reference to "officers" within § 11 of the APA, along with the lack of any express language clearly indicating that Congress intended references to officers in other provisions of the APA to refer to Officers of the United States subject to the Appointments Clause, arguably create ambiguity as to the true nature of agency "examiners." It is a longstanding principle of statutory construction that, "in a case of statutory ambiguity, 'where an otherwise acceptable construction of a statute would raise serious constitutional problems, the Court will construe the statute to avoid such problems unless such construction is plainly contrary to the intent of Congress.'" *Concrete Pipe & Prod.*, 508 U.S. at 628–29 (quoting *Edward J. DeBartolo Corp.*, 485 U.S. at 575). Stated differently, "[w]hen the validity of an act of Congress is drawn in question, and even if a serious doubt of constitutionality is raised, it is a cardinal principle that this Court will first ascertain whether a construction of the statute is fairly possible by which the question may be avoided." *Crowell v. Benson*, 285 U.S. 22, 62 (1932).

Petitioners assert that the APA can only be reasonably construed as having established hearing examiners as Officers of the United States. However, they neglect to advance any argument for why a contrary interpretation would be unreasonable. Petitioners provide no explanation for Congress's omission of the term "officer" from § 11 of the APA—which is specifically dedicated to the detailed discussion of the appointment process for hearing examiners. Petitioners also fail to provide an explanation

for Congress's total omission of any express language clearly indicating that Congress intended references to officers within other provisions of the APA to refer to Officers of the United States subject to the Appointments Clause. Finally, Petitioners neglect to address why Congress would purposefully create an office that it views as being subject to the Appointments Clause, and in the same breath, provide for a process of appointment that facially violates it.

This Court should therefore reject Petitioners' proposed statutory construction in favor of construing the APA as having established hearing examiners as agency employees—thereby avoiding constitutional issues.

III. PETITIONERS' POSITION RENDERS THE "ESTABLISHED BY LAW" PROVISION OF THE APPOINTMENTS CLAUSE SUPERFLUOUS AND WOULD PRODUCE AN ABSURD RESULT.

Petitioners assert that the fact "that SEC ALJs hold offices [E]stablished by [L]aw" and "that they exercise authority . . . deemed sufficiently 'significant'" is sufficient for this Court "to conclude that SEC ALJs are Officers." Pet. Br. at 20; SEC Br. at 16. This definition is too broad and the potential ramifications of Petitioners' position weigh heavily in favor of affirming the decision below. *See Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 749 (1975) ("Thus we conclude that what may be called considerations of policy, which we are free to weigh in deciding this case, are by no means entirely on one side of the scale. Taken together with the precedential support for the Birnbaum rule over a period of more than 20 years, and the consistency of that rule with what we can glean

from the intent of Congress, they lead us to conclude that it is a sound rule and should be followed.").

A. "Established by Law" Should Be Limited to Offices Directly Created by Congress.

Petitioners assert that the office of the SEC ALJs is "established by Law" because it is created by the Administrative Procedure Act. *Id.* at 21 (first citing *Freytag*, 501 U.S. at 881; and then citing *Bandimere v. SEC*, 844 F.3d 1168, 1179 (10th Cir. 2016)). The APA, however, only *permits* "[e]ach agency" to "appoint as many [ALJs] as are necessary for proceedings." 5 U.S.C. § 3105 (2012). The SEC Commission could have decided not to employ this authority. The office of the SEC ALJ only came into existence when the Commission promulgated a rule creating the office. *See* 17 C.F.R. § 200.14 (2017) ("Under the Administrative Procedure Act (5 U.S.C. §§ 551–559) and the federal securities laws, the Office of Administrative Law Judges conducts hearings in proceedings instituted by the Commission."). Thus, insofar as Petitioners assert that the office of the ALJ is "established by Law," Petitioners interpret the term broadly to include any legal authority. *See also* Stephen G. Bradbury, *Officers of the United States Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73, *passim* (2007).

This broad construction of "established by Law" proposed by Petitioners would render this text of the Constitution superfluous. After all, any individual lawfully acting on behalf of the government is acting pursuant to some legal authority. *Cf. Tucker v. Comm'r*, 135 T.C. 114, 157–58 (2010) ("[A]ny 'Office' that actually exists in the

Federal Government is arguably 'established by Law.'"). For example, FBI investigators are "officials" whose appointment is authorized by statute. *See* 28 U.S.C. § 533 (2012). The Appointments Clause, however, pertains to "all other Officers of the United States . . . which shall be established by Law." U.S. Const. art. II, § 2, cl. 2. Plainly, then, the text of the Constitution suggests that some federal Officers to be established by "Law" and some officers to act not pursuant to any "Law." If law is to be understood to include rules, regulations and other legal authority, then all federal offices are established by law. Thus, the "established by Law" clause would become mere surplusage, which is an impermissible interpretation of the Constitution. *Tucker*, 135 T.C. at 157; *cf. Hibbs v. Winn*, 542 U.S. 88, 101 (2004) (holding that statutes should not be read to render any portion of the text superfluous).

A more sound approach is to limit the application of the Appointments Clause to offices directly created by Congress. In fact, this Court found individuals to be Officers of the United States primarily in cases where the office they held was created directly by statute rather than by regulation or executive action. *See Free Enter. Fund v. PCAOB*, 561 U.S. 477, 484–85 (2010) (the Public Company Accounting Oversight Board created under the Sarbanes-Oxley Act); *Freytag*, 501 U.S. at 870 (the Tax Court created under 26 U.S.C. § 7441, which provided that "[t]here is hereby established . . . the United States Tax Court."); *Morrison v. Olson*, 487 U.S. 654, 660–61 (1988) (the "independent counsel" created under the Ethics in Government Act in instances where high-ranking government officials are investigated); *Buckley*, 424 U.S. at 7 (the Federal Election Commission established under the Federal Election Campaign Act); *Humphrey's*

Ex'r v. United States, 295 U.S. 602, 619–20 (1935) (the Federal Trade Commission created by the Federal Trade Commission Act). Accordingly, the Court should interpret the "established by Law" requirement to only apply to offices created directly by Congress. This interpretation gives adequate effect to the text of the Constitution.

B. Petitioners' Overly Broad Definition of Officers Would Produce an Absurd Result.

Second, Petitioners' definition for Officers of the United States is overbroad and would produce an absurd result because it would apply constitutional requirements to SROs. *See Pub. Citizen v. Dep't of Justice*, 491 U.S. 440, 454 (1989) ("Where the literal reading of a statutory term would compel 'an odd result,' . . . we must search for other evidence of congressional intent to lend the term its proper scope."). Under Petitioners' definition, any office holder is an Officer of the United States so long as that office exists pursuant to any legal authority, *see supra* subpart I.C.*i.*, and must perform significant functions, *see* Pet. Br. at 20–23; SEC Br. at 16. According to Petitioners, the SEC ALJs perform significant functions because they can amend charging documents, enter default judgments, consolidate proceedings, issue subpoenas, order depositions, regulate the hearing, rule on admissibility, and take other necessary steps towards an initial decision. Pet. Br. at 21–23. All parties agree that any action by the ALJ is subject to review by the Commission. 15 U.S.C. § 78d-1(b). Thus, any action of the ALJ remains initial until affirmed by higher authority.

Petitioners' position is overbroad because factfinders within FINRA may satisfy both prongs

of Petitioners' definition. *See* Joseph McLaughlin, *Is FINRA Constitutional?*, 12 Engage, Sept. 2011, at 111, 111–14; Robert Botkin, Note, *FINRA and the Developing Appointments Clause Doctrine*, 17 Wake Forest J. Bus. & Intell. Prop. L. 627, 630–43 (2017).

FINRA satisfies the first prong of Petitioners' definition because its operation is authorized by law. "FINRA is not part of the government"; it is "a not-for-profit organization authorized by Congress to protect America's investors." *About FINRA*, Fin. Indus. Regulatory Auth. (2018).[3] It is authorized under 18 U.S.C. § 78*o*-3 to promote just and equitable principles of trade" by "appropriately discplin[ing] their members for violations of any provision of the Exchange Act, the rules or regulations promulgated thereunder, or their own rules." *Fiero v. Fin. Indus. Regulatory Auth., Inc.*, 660 F.3d 569, 574 (2d Cir. 2011) (quoting 15 U.S.C. § 78*o*-3(b)(7)). FINRA is thus authorized by statute, and its disciplinary actions are likewise authorized by statute. Accordingly, under Petitioners' definition, FINRA and its hearing officers would be "established by Law."

FINRA also satisfies the second prong of Petitioners' definition. It is widely recognized that FINRA plays a key role in regulating the securities industry. It "perform[s] much of the day-to-day oversight of the securities markets and Broker-Dealers under their jurisdiction. [FINRA is] primarily responsible for establishing standards under which members conduct business; monitoring how that business is conduct; and bringing disciplinary actions against members for violating applicable federal statutes,

3. https://www.finra.org/about.

SEC rules, and [FINRA] rules." U.S. Gov't Accountability Off., GAO-15-376, *Securities Regulation: SEC Can Further Enhance Its Oversight Program of FINRA* 1 (2015). With regards to disciplinary proceedings, FINRA disciplinary hearing officers function similarly to ALJs. FINRA hearing officers can compel production of evidence or direct witnesses to give a statement. *See Guide to the Disciplinary Hearings Process*, Fin. Indus. Regulatory Auth..[4] At the hearing, FINRA hearing officers direct the proceeding, determine the admissibility of evidence, compile the record, and issue an initial decision. *Id.* Much like a defendant in an SEC proceeding can appeal to the district court, a defendant before FINRA retains the right to appeal to the National Adjudicatory Council and, thereafter, to the SEC. *Id.*; *see also* 15 U.S.C. § 78s(e)(1) (2012). Accordingly, FINRA hearing officers perform the same functions Petitioners allege are substantial enough to be deemed an Officer of the United States. As FINRA hearing officers satisfy both prongs of Petitioners' definition, they would need to be appointed pursuant to the Appointments Clause if Petitioners' argument were adopted by this Court.

There is no serious question, however, that FINRA disciplinary hearing officers need not be appointed pursuant to the Appointments Clause. FINRA hearing officers are attorneys employed by FINRA. *See Answers to Frequently Asked Questions for Respondents in FINRA Disciplinary Proceedings*, Fin. Indus. Regulatory Auth.[5]

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4. http://www.finra.org/industry/guide-disciplinary-hearing-process#proceedings

5. http://www.finra.org/industry/faq-disciplinary-proceedings

They are not appointed by the President, the courts, or by a head of any department. In fact, FINRA disciplinary officers could not be so appointed because "FINRA is not part of the government." *About FINRA*, *supra*. FINRA is headed by a board of governors who are elected by securities dealers. *See FINRA Manual* art. vii, §§ 4(a), 13 (2011).[6] Accordingly, if the Court accepts Petitioners' position, FINRA hearing officers would exist in violation of the Appointments Clause even though that plainly is not so under established law.

This absurd potential effect on FINRA disciplinary hearing officers shows that Petitioners' position is overbroad. For one, the effect undermines this Court's precedent. FINRA, after all, is an SRO and not a federal agency. *See, e.g.*, *PCAOB*, 561 U.S. at 484–85 (2010) (contrasting SROs like the New York Stock Exchange with federal agencies); *North v. Smarsh, Inc.*, 160 F. Supp. 3d 63, 78 (D.D.C. 2015). This Court held that for such non-government entities to be recognized as a "part of the Government for purposes of the [Constitution]," Congress must retain control over the SRO's executive board. *Lebron v. Nat'l R.R. Passenger Corp.*, 513 U.S. 374, 400 (1995); *see also Horvath v. Westport Library Ass'n*, 362 F.3d 147, 153 (2d Cir. 2004). Congress did not retain such control over FINRA's board of governors—they are elected by their members. *See FINRA Manual*, *supra*, at art. vii, §§ 4(a), 13. Thus, Petitioners' position would undermine *Lebron*, by subjecting some non-government entities to the requirements of the Constitution, even when

6. http://finra.complinet.com/en/display/display_viewall.html?rbid=2403&element_id=4628&record_id=6028&filtered_tag=

Congress does not retain control over the organizations' boards. Notably, this would not affect only FINRA, but potentially other SROs as well. *See, e.g.*, 7 U.S.C. § 12a(3)(J) (2012) (SROs in the commodity exchange market).

Second, the Petitioners' definition seriously affects FINRA's ability to perform its SRO functions. FINRA oversees over "3,900 brokerage firms, more than 160,000 branch offices and nearly 635,000 registered representatives." Botkin, *supra*, at 637. In 2017 alone, FINRA resolved 3,735 cases. *See Dispute Resolution Statistics*, Fin. Indus. Regulatory Auth. (Feb. 24, 2018).[7] This is more than five times as many cases as the SEC adjudicated during the same time period. SEC, Div. of Enfm't, *Annual Report: A Look Back at Fiscal Year* 2017 at 6 (2017).[8] As a result of Petitioners position, FINRA hearing officers would need to be appointed pursuant to the Appointments Clause—hindering, or eliminating completely, the ability of FINRA to perform its self-regulatory functions.

* * *

Petitioners' position is thus overbroad in two important ways: it threatens to render the "established by Law" provision of the Appointments Clause superfluous; and, it threatens to disrupt the regulatory functions of SROs. To avoid the ramifications discussed above, the Court should affirm the decision below. *See Blue Chip Stamps*, 421 U.S. at 749.

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7. http://www.finra.org/arbitration-and-mediation/dispute-resolution-statistics

8. https://www.sec.gov/files/enforcement-annual-report-2017.pdf

IV. EVEN IF SEC ALJS ARE OFFICERS, REMAND, RATHER THAN DISMISSAL, IS THE APPROPRIATE REMEDY.

If this Court determines that SEC ALJs are Officers under the Appointments Clause, then remand to a duly appointed panel is the correct remedy, as Petitioners assert. *See* Pet. Br. at 43–49. Where Petitioners err is in claiming that dismissal is warranted. *See id.* at 49–58. There are no legal grounds to dismiss the action against Petitioners. In cases involving improperly appointed adjudicators, this Court has held that remand to a duly appointed adjudicator was the remedy, not dismissal. *See Ryder v. United States*, 515 U.S. 177, 188 (1995) ("Petitioner is entitled to a hearing before a properly appointed panel of that court."). After all, the judgment of a tribunal improperly appointed is not, in itself, invalid. *See Ex parte Ward*, 173 U.S. 452, 456 (1899) ("The result of the authorities is that the title of a person acting with color of authority, even if he be not a good officer in point of law, cannot be collaterally attacked. . . ."). In general, the judgment will stand regardless under the de facto officer doctrine. *Id.* While Petitioners argue they suffered a constitutional wrong, *see Ryder*, 515 U.S. at 182, the alleged defect was in the process rather than in the disposition of the merits—a duly appointed tribunal may have come to the same conclusion as the ALJs. Accordingly, Petitioner may be entitled to correct process, but not to the dismissal of the complaint.

Petitioners do not cite any law to the contrary. In fact, their entire argument for dismissal is based on the fact that a new ALJ may once again find against them, *see* Pet. Br. at 49–50, and that the long years defending against

the Commission has left him destitute, *see id.* at 57–58 ("Lucia fought the good fight."). While that may certainly be true, remand is the remedy this Court has used in similar situations. *See, e.g.*, *Elchuk v. United States*, 310 F.2d 717, 717 (5th Cir. 1962) (affirming earlier decision after remand from the Supreme Court); *Goldbaum v. United States*, 222 F.2d 360, 361 (9th Cir. 1955) (same).

CONCLUSION

For the aforementioned reasons, the decision of the U.S. Court of Appeals for the District of Columbia Circuit should be affirmed.

Dated: April 2, 2018

Respectfully submitted,

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No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, ET AL.,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF FOR COURT-APPOINTED *AMICUS CURIAE* IN SUPPORT OF THE JUDGMENT BELOW

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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INTEREST OF *AMICUS CURIAE*

By order dated January 18, 2018, this Court invited Anton Metlitsky to brief and argue this case as *amicus curiae* in support of the judgment below. The court below held that administrative law judges of the Securities and Exchange Commission are not "Officers of the United States" under the Appointments Clause of the United States Constitution.[1]

RELEVANT CONSTITUTIONAL, STATUTORY, AND REGULATORY PROVISIONS

Relevant constitutional, statutory, and regulatory provisions are reproduced in the appendix to this brief.

STATEMENT OF THE CASE

The Appointments Clause regulates the means of appointment of "Officers of the United States." U.S. Const. art. II, § 2, cl. 2. "Principal" officers must be appointed by the President "by and with the Advice and Consent of the Senate." *Id.* Congress may also provide for "inferior Officers" to be appointed in that manner, but alternatively may "vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments." *Id.*

The Appointments Clause is primarily "designed to preserve political accountability relative to important Government assignments." *Edmond v.*

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[1] No counsel for a party authored this brief in whole or in part, and no person other than *amicus curiae* and his firm made a monetary contribution to this brief's preparation or submission.

United States, 520 U.S. 651, 663 (1997). In light of that purpose, the "Officers of the United States" who must be appointed in the manner required by the Clause include only those persons who both hold a continuing government position "established by [federal] Law," U.S. Const. art. II, § 2, cl. 2, and who have the authority, in their own name, to "bind[] the government or third parties for the benefit of the public," *Officers of the United States Within the Meaning of the Appointments Clause*, 31 Op. O.L.C. 73, 77 (2007) ("2007 OLC Op."). In this way, federal appointees authorized to "exercise the power of the United States" by binding the government or private parties are "accountable to the President"—either directly or through a senior official who is himself a presidential appointee—and the President is in turn "accountable to the people." *Dep't of Transp. v. Ass'n of Am. R.Rs.*, 135 S. Ct. 1225, 1238 (2015) (Alito, J., concurring).

By contrast, "a person whose acts have no authority and power of a public act or law absent the subsequent sanction of an officer or the legislature"—for example, a person exercising "advisory" or "investigative" functions—is not an "Officer of the United States" but an employee. 2007 OLC Op. 95, 98 (quotations omitted). The overwhelming majority of those working in the Executive Branch are mere employees—i.e., "lesser functionaries subordinate to officers of the United States," *Buckley v. Valeo*, 424 U.S. 1, 126 n.162 (1976)—who need not be appointed under the Appointments Clause. In 1879, this Court estimated that 90% of all federal workers were "undoubtedly" employees, not officers. *United States v.*

Germaine, 99 U.S. 508, 509 (1879). By 2010, "[t]he applicable proportion" of non-officer employees had "of course increased dramatically." *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 506 n.9 (2010).

The question presented in this case is whether administrative law judges ("ALJs") employed by the Securities and Exchange Commission ("SEC" or "Commission") are inferior "Officers of the United States," such that they must be appointed in conformity with the Appointments Clause. Pet. i. The background relevant to answering the question presented is as follows:

A. Administrative Law Judges And The Administrative Procedure Act

1. The "rapid growth of administrative law" beginning in the early Twentieth Century increased the number of agency hearings to the point that "the agency heads ... [could] rarely preside over hearings in which evidence is required." *Ramspeck v. Fed. Trial Exam'rs Conf.*, 345 U.S. 128, 130 (1953). "The agencies met this problem ... by designating hearing or trial examiners to preside over hearings for the reception of evidence." *Id.* at 130-31; *see also* Paul Verkuil et al., *The Federal Administrative Judiciary*, Admin. Conf. of the United States, Recommendations and Reports, Vol. II, 1992 ACUS 770, 799 (1992) ("hearing examiners presided at adjudications before enactment of the [Administrative Procedure Act ('APA')], and the term 'examiner' was used at least as early as 1906"). Those examiners "made a report to the agency setting forth proposed findings of fact and recommended action," with the "final de-

cision" left to the agency heads. *Ramspeck*, 345 U.S. at 131.

Before Congress enacted the APA, employing agencies themselves determined hearing examiners' compensation and promotion under the Classification Act of 1923, placing the examiners in a "dependent status" to those agencies. *Id.* at 130. This resulted in "[m]any complaints ... against the actions of the hearing examiners, it being charged that they were mere tools of the agency concerned and subservient to the agency heads in making their proposed findings of fact and recommendations." *Id.* at 131.

2. Congress in the APA sought to address concerns about the independence of hearing examiners—known today as ALJs[2]—and considered "the securing of fair and competent hearing personnel ... the heart of formal administrative adjudication." *Butz v. Economou*, 438 U.S. 478, 514 (1978) (quotation omitted). The APA thus "contains a number of provisions designed to guarantee the independence of [ALJs]." *Id.*

In particular, Congress "intended to make hearing examiners a special class of semi-independent subordinate hearing officers by vesting control of their compensation, promotion and tenure in the Civil Service Commission to a much greater extent than in the case of other federal employees." *Ramspeck*, 345 U.S. at 132 (quotation omitted).

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[2] Hearing examiners were first referred to as "administrative law judges" by regulation in 1972, 37 Fed. Reg. 16,787 (Aug. 19, 1972), and then by statute in 1978, Pub. L. No. 95-251, 92 Stat. 183 (1978).

Thus, "[e]ach agency" may "appoint" ALJs, 5 U.S.C. § 3105, but the Office of Personnel Management ("OPM")—formerly the Civil Service Commission—determines who is qualified to hold that position, *id.* § 5372. Agencies have no authority to alter an ALJ's salary, *id.*, and no "action" (including removal) can be taken by the agency against the ALJ except "for good cause established and determined by the Merit Systems Protection Board," *id.* § 7521(a).

3. Although the APA granted ALJs *structural* independence from their employing agencies, it did not grant them any independent policymaking or decisional authority, instead ensuring that ALJs remain "subordinate" to their agencies. *Ramspeck*, 345 U.S. at 132; *see also* 5 U.S.C. § 557(c) (referring to ALJs as "subordinate employees"). Thus, as a general matter, the APA authorizes ALJs to "preside at the taking of evidence" in formal adjudications, 5 U.S.C. § 556(b)—which includes the power, for example, to "issue subpoenas," "receive relevant evidence," and "regulate the course of the hearing," *id.* § 556(c)—and to issue "initial decision[s]," *id.* § 557(b). But the Act also ensures that on "appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision" itself. *Id.*

Thus, the agency has final and plenary authority over ALJ decisions not only as to questions of law but also as to questions of fact. *See FCC v. Allentown Broad. Co.*, 349 U.S. 358, 364-65 (1955). The APA, in other words, ensures that evidence is taken and facts are determined "in the first instance by an official not subject to agency coercion," but that "the

agency retains full power over policy, a power it can exercise when it performs its reviewing function." 1992 ACUS at 803; *see also Attorney General's Manual on the Administrative Procedure Act* 83 (1947) (agency "is in no way bound by the decision" of ALJ and "retains complete freedom of decision—as though it had heard the evidence itself").

4. Congress has defined the terms "officer" and "employee" as used in Title 5 of the U.S. Code. The statutory definition of "officer" includes only individuals who must be appointed in the manner provided by the Appointments Clause, 5 U.S.C. § 2104, while the definition of "employee" includes officers and those appointed by, among others, "an individual who is an employee under this section," *id.* § 2105(a)(1)(D). Title 5 refers to ALJs as "employees." *See, e.g., id.* § 556(c) ("employees presiding at hearings"); *id.* § 557(b) ("presiding employee").

B. Securities And Exchange Commission ALJs

The question presented in this case turns on the powers of the ALJs employed by the SEC. Pet. i.[3] The duties and authority of SEC ALJs are set forth in SEC regulations promulgated under authority Congress has granted the SEC.

1. The SEC is a five-member independent agency whose members the President appoints by and

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[3] As petitioners note, there are nearly 2,000 ALJs across the federal government, many of whom appear to exercise functions different from those of SEC ALJs. Pet. Br. 41-42. Whether ALJs other than SEC ALJs are "Officers of the United States" is not at issue here.

with the advice and consent of the Senate. *See* 15 U.S.C. § 78d(a). Among other functions, the Commission is empowered to enforce federal securities laws and regulations. *See, e.g., id.* § 78d. One mechanism for SEC enforcement is an administrative action within the Commission. 17 C.F.R. § 202.5(b).

The Commission itself is authorized by 5 U.S.C. § 3105 to appoint ALJs to preside over such hearings. Since 1962, however, Congress has authorized the Commission to delegate "any of its functions" other than rulemaking to "a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee board." 15 U.S.C. § 78d-1(a); *see* Pub. L. No. 87-592, 76 Stat. 394, 394-95 (1962). The Commission under this authority had (until recently) delegated the power to hire ALJs to SEC staff, who typically chose from a list of qualified candidates provided by OPM.[4] Pet. App. 295a-297a.[5]

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[4] Cameron Elliot, the ALJ who presided below, was an ALJ at the Social Security Administration before the SEC, and he may have been hired by the SEC under a process somewhat different from that described above. Notice at 2, *In re Timbervest LLC*, No. 3-15519 (SEC June 23, 2015) (filed by SEC Enforcement Division), https://perma.cc/5RMX-R6V4. It is undisputed, however, that ALJ Elliot was "hired without the involvement of individual Commissioners." *Id.*

[5] On November 30, 2017, the Commission "ratified" the appointment of its current ALJs, including the ALJ who presided over petitioners' hearing, and ordered a reopening of the record in all cases then still pending before the SEC. *See* SEC, Order (Nov. 30, 2017), https://www.sec.gov/litigation/opinions/2017/33-10440.pdf. The Commission took no action, however,

2. a. The SEC has delegated certain authorities to its ALJs under the statute just described, which authorizes the Commission to delegate "any of its [non-rulemaking] functions" to (among others) ALJs. 15 U.S.C. § 78d-1(a). Subsection (b) of that statute provides that the "Commission shall retain a discretionary right to review the [delegated] action ... upon its own initiative or upon petition," and lists circumstances in which Commission review is mandatory. *Id.* § 78d-1(b). Subsection (c) provides that if plenary discretionary review of delegated functions is not sought or undertaken, "then the action of any" delegee (including an ALJ) listed in subsection (a) "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." *Id.* § 78d-1(c).

ALJs' authority is thus limited by the scope of delegation from the Commission. By regulation, "[a]ll proceedings shall be presided over by the Commission or, if the Commission so orders, by a hearing officer." 17 C.F.R. § 201.110. The "hearing officer" may be, among others, an ALJ. *Id.* § 201.101(a)(5). ALJs are responsible for "conduct[ing] hearings" and for ensuring "the fair and orderly conduct of the proceedings." *Id.* § 200.14(a). And the Commission grants ALJs "the authority to do all things necessary and appropriate to discharge [their] duties," including administering oaths, receiving evidence, ruling on motions, issuing subpoenas,

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with respect to cases (like this one) in which a petition for judicial review had already been filed. *See* Resp. Br. 3 n.2.

and issuing an initial decision on whether the securities laws have been violated. *Id.* § 201.111.

b. The Commission, however, has not delegated ALJs authority to bind the government or private parties. Rather, as the SEC explained in the proceedings below, the Commission retains "plenary authority over the course of ... administrative proceedings and the rulings of [its] law judges—before and after the issuance of the initial decision and irrespective of whether any party has sought relief." Pet. App. 91a (quotation omitted).

For instance, although ALJs may issue subpoenas, *see* 17 C.F.R. §§ 200.14(a)(2), 201.111, they cannot enforce them—only a federal district court can enforce an SEC subpoena, including by contempt, and only at the request of the Commission itself. 15 U.S.C. § 78u(c). The only authority the ALJ has to punish "[c]ontemptuous conduct" is to exclude the offender from the hearing room or preclude her from representing a party in the proceeding—actions that are subject to immediate *de novo* review by the Commission. 17 C.F.R. § 201.180(a)(1), (2).

ALJs also lack authority to issue a decision on the merits that binds the Commission or private parties. Rather, the ALJ prepares an "initial decision," which "include[s] findings and conclusions, and the reasons or basis therefor, as to all the material issues of fact, law or discretion presented on the record and the appropriate order, sanction, relief, or denial thereof." *Id.* § 201.360(b). The Commission "may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part," any initial decision. *Id.* § 201.411(a). The Commission may

"make any findings or conclusions that in its judgment are proper and on the basis of the record." *Id.* The Commission's review is *de novo* as to both law and facts. *Id.*; *see* 15 U.S.C. § 78d-1(b). And while the Commission as a matter of practice accords "considerable weight" to some ALJ credibility findings, it does not accept such findings "blindly," Pet. App. 92a-93a n.117 (quotation omitted), and is under no legal obligation to accept or defer to those findings at all, *see* 17 C.F.R. §§ 201.411(a), 201.452.

Finally, the Commission's review is not limited to the record before the ALJ. Rather, the Commission may—as it did in this case, *see infra* at 12—remand the matter to the ALJ "for further proceedings," 17 C.F.R. § 201.411(a), including "the taking of additional evidence," *id.* § 201.452, and may even elect to "accept or hear additional evidence" itself, *id.*

c. Notably, no ALJ initial decision can become final without a subsequent affirmative act of the Commission. The Commission will review an ALJ's initial decision on a petition for review, *id.* § 201.411(b), and can do so *sua sponte* if no petition is filed, *id.* § 201.411(c). Even if the Commission decides not to conduct plenary review, the ALJ's decision does not automatically become final, nor does it otherwise carry any force of its own. Rather, no initial decision by an ALJ becomes final until the Commission enters its own finality order. *Id.* § 201.360(d)(2). Moreover, were the Commission ever to delegate to ALJs the authority to issue a decision that took effect without the Commission's affirmative sanction, that decision would, by operation

of statute, be the decision of the Commission, not the ALJ. *See* 15 U.S.C. § 78d-1(c).

Thus, contrary to petitioners' assertion that an SEC ALJ decision becomes final even if it is not "affirmatively adopted by the agency," Pet. Br. 32, no initial decision becomes final simply because of "the lapse of time"; it is "the Commission's issuance of a finality order" that makes an initial decision not selected for plenary review "effective and final." Pet. App. 90a (quotation omitted). As the Commission emphasized below, the "effect of this rule ... is that [SEC] ALJs' initial decisions ... do not become the final and effective decision of the agency without affirmative action on [the Commission's] part—specifically, [its] issuance of a finality order." Pet. App. 90a n.109.

The same is true if an ALJ finds a party to be in "default." 17 C.F.R. § 201.155. An initial decision based on default has no effect absent further action by the Commission. *See In re Alchemy Ventures, Inc.*, 2013 WL 6173809, at *4 (SEC Oct. 17, 2013); 17 C.F.R. § 201.360(d)(2).[6]

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[6] Petitioners state that "[i]n about 90% of cases, ... the ALJ's initial decision 'become[s] final without plenary agency review.'" Pet. Br. 32 (quoting *Bandimere v. SEC*, 844 F.3d 1168, 1180 n.25 (10th Cir. 2016)). SEC Commissioner Jackson recently provided context for that statistic. During 2014 and 2015, 80% of all SEC ALJ decisions arose from a default, and in the remainder of initial decisions that did not receive plenary review, no petition for review was filed. Review was sought in approximately 10% of cases, and granted in every one of those. Robert J. Jackson, Jr., *Fact and Fiction: The SEC's Oversight of Administrative Law Judges*, The CLS Blue Sky Blog (Mar. 9, 2018), https://perma.cc/EM5Y-B7R2.

C. Proceedings Before The Commission

1. On September 5, 2012, the Commission instituted administrative proceedings against petitioners for four alleged violations of the Investment Advisers Act. *See In re Raymond J. Lucia Cos.*, 2012 WL 3838150 (Sept. 5, 2012). The Commission assigned ALJ Elliot to oversee the initial stages of the proceeding. *See id.*

After the ALJ issued an initial decision concluding that petitioners had violated the securities laws as to one of the four charges and recommending sanctions, *see In re Raymond J. Lucia Cos.*, 2013 WL 3379719 (July 8, 2013), the Commission *sua sponte* remanded the case for further findings on the three charges the ALJ did not address in that initial decision, concluding that "even if no party chooses to seek review, the law judge's findings would assist [the Commission's] determination of whether to order review on [its] own initiative," Pet. App. 242a.

The ALJ subsequently issued a revised initial decision, considering the additional three charges and concluding that "[t]he sanction determinations made in the [original initial decision] remain[ed] appropriate." Pet. App. 118a.

2. a. Both petitioners and the SEC Division of Enforcement petitioned for review. The Commission granted review and concluded, based "on an independent review of the record," except as to unchallenged factual findings, that petitioners violated the securities laws and imposed the sanctions recommended by the ALJ. Pet. App. 39a-40a.

b. The Commission also rejected petitioners' argument that the ALJ's initial decision was void because the ALJ was an "Officer of the United States," concluding that "the appointment of Commission ALJs is not subject to the requirements of the Appointments Clause," Pet. App. 86a, because they are employees, not constitutional officers, *see* Pet. App. 86a-95a.

Two Commissioners dissented on the merits, and also noted that an Article III court should decide the Appointments Clause issue. Pet. App. 110a-114a.

D. Proceedings Below

The court of appeals denied petitioners' petition for review of the Commission's decision, including their Appointments Clause challenge.

The court explained that SEC ALJs are not "Officers of the United States" required to be appointed in conformity with the Appointments Clause because they have not "been delegated sovereign authority to act independently of the Commission," and do not "have the power to bind third parties, or the government itself, for the public benefit." Pet. App. 16a. SEC ALJs, the court reasoned, cannot issue any decision that becomes final absent affirmative Commission action. Pet. App. 14a-15a. And ultimate decision-making authority in all events remains with the Commission: the Commission reviews ALJs' initial decisions *de novo* and it "may make any findings or conclusions that in its judgment are proper and on the basis of the record," Pet. App. 18a-19a (quoting 17 C.F.R. § 201.411(a)); the Commission "controls

the record for review and decides what is in the record," Pet. App. 19a (quotation omitted); the Commission "may 'remand for further proceedings,'" *id.* (quoting 17 C.F.R. § 201.411(a)), or "the taking of additional evidence," *id.* (quoting 17 C.F.R. § 201.452); and the Commission may "hear additional evidence" itself, *id.* (quoting 17 C.F.R. § 201.452). Moreover, "the Commission may defer to [ALJs'] credibility determinations where the record provides no basis for disturbing the finding, but ... is not required to adopt the credibility determinations of [the] ALJ." *Id.* (citing *Kay v. FCC*, 396 F.3d 1184, 1189 (D.C. Cir. 2005)).

The court of appeals granted rehearing en banc, Pet. App. 244a-246a, but denied the petition for review by an equally divided court, Pet. App. 1a-2a.

SUMMARY OF ARGUMENT

I. A federal appointee is an "Officer of the United States" under the Appointments Clause if she holds a continuing position established by federal law (which is undisputed here) and she has been delegated (i) the power to bind the government or private parties (ii) in her own name rather than in the name of a superior officer.

A. The consistent understanding of Congress, the Executive Branch, and knowledgeable observers since the Founding era is that an individual is an "Officer of the United States" only if (among other things) she has been delegated a portion of the sovereign authority of the United States, meaning that she can bind the government or alter the rights of private parties. Persons whose acts have no force

absent the subsequent sanction of a superior officer, in contrast, are not constitutional officers.

Thus, for example, persons who can authoritatively interpret the law, bring enforcement actions and make litigation decisions on behalf of the United States, promulgate regulations, or issue decisions binding on private parties may be constitutional officers. It has been established since at least the Nineteenth Century, however, that persons who perform investigative functions but can only make recommendations based on the results of their investigation are not officers. That is so even if those individuals have power to perform hearing-related functions such as issuing subpoenas, administering oaths, taking testimony, and receiving documents.

That result is fully consistent with this Court's precedent.

B. It has also been understood since the First Congress, and this Court's cases confirm, that even an individual who has de facto authority to bind the government or alter private-party rights is not a constitutional officer for purposes of the Appointments Clause if she can only exercise that authority in the name of a superior officer rather than in her own name. Such an individual is considered an agent of a principal who is a constitutional officer, not an officer herself. The principal—i.e., the constitutional officer—will be held accountable for the acts of the agent done in the principal's name.

C. This Court's modern cases have described constitutional officers as those who exercise "significant authority pursuant to the laws of the United

States." *Buckley*, 424 U.S. at 126. Although the Court has not had occasion to flesh out the precise contours of that standard, it is fully consistent with the longstanding historical rule just described.

Petitioners and the Solicitor General argue for a substantially broader understanding of officer status, relying on a portion of this Court's opinion in *Freytag v. Commissioner*, 501 U.S. 868 (1991), that describes as "significant" certain hearing-related functions of the Tax Court special trial judges at issue there—i.e., taking testimony, conducting trials, ruling on the admissibility of evidence, and enforcing compliance with discovery orders. Some of these functions bind neither the government nor private parties, so the Court's opinion could be read as adopting a broader understanding of officer status inconsistent with the longstanding view described above. But *Freytag*'s holding is fully consistent with that longstanding view, and this Court should not construe the opinion more broadly, for several reasons.

First, the special trial judges in *Freytag* could bind the government and private parties by issuing final judgments in their own name in some circumstances. It is true that language in the Court's opinion suggests that the Court might have viewed the hearing-related functions described in the previous paragraph as by themselves sufficient to make special trial judges constitutional officers, even absent the ability to enter final binding judgments. But that language was unnecessary to the holding in *Freytag*, and in any event, even those hearing-related functions included the ability to bind the

government and private parties, because special trial judges have the authority to enforce their own discovery orders by punishing contempt. While other functions set forth in the opinion—such as ruling on the admissibility of evidence—are unrelated to any enforcement authority, the Court did not consider whether such powers alone would suffice to establish officer status, and there is no basis to read *Freytag* broadly to indicate that they would, inconsistent with the historical understanding described above.

Second, not only could petitioners' standard call into question the constitutionality of the appointment process of untold number of federal actors who perform "significant" functions, it would also cast significant doubt on the constitutionality of the more-than-a-century-old practice of establishing investigative commissions whose members, including members of Congress, are not appointed in the manner prescribed by the Appointments Clause. These commissions generally do not have the power to punish contempt, but do have the power to issue subpoenas, administer oaths, examine witnesses, and receive documents—i.e., similar powers to those exercised by the special trial judges in *Freytag* (and SEC ALJs). Despite these powers, both Congress and the Executive Branch have repeatedly concluded that so long as a commission can only make recommendations based on the results of the investigation but not act on those recommendations—for example, by promulgating a regulation—the commission members are not constitutional officers. That conclusion is crucial not only for purposes of the Appointments Clause, but also because the Incompati-

bility Clause, U.S. Const. art. I, § 6, cl. 2, prevents members of Congress from being appointed to federal "Offices." Petitioners' understanding of *Freytag* would likely preclude members of Congress from serving on such commissions, and invalidate more than one hundred years of consistent practice and understanding.

Third, limiting officers to persons who have authority to bind the government or private parties in their own name furthers the purpose of the Appointments Clause. The President (directly or through his direct subordinates) is appropriately held to account for persons who bind the government or private parties in their own name. But there is no reason to hold the President accountable for those whose acts require subsequent sanction by a superior—or those who can act only in a superior's name—because the President will be held accountable for the acts of the officer who grants subsequent sanction or in whose name the act is done.

Fourth, the historical understanding provides Congress and the President an administrable rule for determining when the Appointments Clause and other provisions that turn on officer status (such as the Foreign Emoluments Clause) apply. A rule that hinges officer status on the "significance" (in a colloquial sense) of a person's functions would make it difficult for Congress and the President to structure the government consistent with those provisions.

II. SEC ALJs are not constitutional officers because, although they occupy continuing positions in the federal government established by law, they sat-

isfy neither of the traditional rule's other necessary prerequisites for officer status.

A. An SEC ALJ has no authority to bind the Commission in any respect because the Commission can review any ALJ decision or determination—including credibility findings and decisions about what constitutes the record—*de novo*. The fact that the Commission sometimes chooses to defer to an ALJ's credibility determinations even though it is not required to do so is irrelevant, because what matters is whether the Commission is *bound* by any ALJ act. It is not.

Nor can SEC ALJs alter the rights of private parties (or bind the Commission) by entering final decisions—even in cases when the Commission does not conduct plenary review, an ALJ decision has no force at all until the Commission affirmatively enters a finality order. The Solicitor General contends that despite the Commission's finality-order requirement, an ALJ initial decision that the Commission decides not to review *de novo is* a final decision of the ALJ because it "shall, for all purposes ... be deemed the action of the Commission." 15 U.S.C. § 78d-1(c). That is wrong for two reasons. First, § 78d-1(c) only applies to actions that the Commission has delegated ALJs the authority to perform in the first place, and the Commission has not delegated ALJs the authority to enter decisions that have any effect without affirmative Commission adoption. Second, even if the Solicitor General's understanding of subsection (c) were correct, all final decisions under that provision are issued in *the Commission's* name, not the ALJ's. The ALJ, in other words, acts

only as the Commission's agent, and the fact that every final decision is entered in the Commission's name ensures that it is the Commissioners who are held accountable.

Petitioners also argue that SEC ALJs are constitutional officers even absent the power to enter binding decisions because SEC ALJs possess hearing-related powers similar to those of the special trial judges in *Freytag*, including the power to issue subpoenas, swear oaths, and receive evidence. But those are not functions limited to constitutional officers. And ALJs have no authority to punish contempt (or do anything else) in a manner that alters a party's legal rights.

Moreover, although SEC ALJs share some features in common with Article III judges and other adjudicators the Court has held are constitutional officers, the powers that render those persons officers—e.g., the power to enter binding judgments and punish contempt—are powers that SEC ALJs lack.

B. Holding that SEC ALJs are employees rather than officers promotes the core accountability purpose of the Appointments Clause because no SEC ALJ decision has binding effect absent affirmative Commission action, and every binding decision is made in the Commission's name. The Commissioners will thus be held fully accountable for those decisions.

C. Nothing in the APA or the securities laws suggests that Congress understood ALJs in general or SEC ALJs in particular to be constitutional officers. To the contrary, every indication is that Con-

gress has always understood that ALJs are civil-service employees, not "Officers of the United States."

III. If this Court holds that SEC ALJs are constitutional officers, petitioners present an argument about the appropriate remedy for an Appointments Clause violation, and the Solicitor General asks the Court to decide whether restrictions on ALJs' removal are constitutional (or whether a serious constitutional question can be avoided by narrowly construing those restrictions). The Court has not invited Court-appointed *amicus* to take a position on either question, because neither implicates arguments "in support of the judgment below." 138 S. Ct. 923. Moreover, the Court did not add a question presented concerning the removal question despite requests that it do so, indicating that the removal question is not properly before the Court.

ARGUMENT

The Appointments Clause requires that "Officers of the United States" be appointed by the President with the advice and consent of the Senate, except that Congress may alternatively provide that "inferior Officers" be appointed by the President alone, the Head of a Department, or a Court of Law. U.S. Const. art. II, § 2, cl. 2. The ALJ who presided over petitioners' hearing, and the SEC's other ALJs, were not initially appointed in any of those ways, but instead were selected by SEC staff under authority delegated from the Commission. *See supra* at 7. The question presented is whether that manner of appointing SEC ALJs is unlawful because they are constitutional officers. The answer is no.

As the parties ultimately agree, the question whether SEC ALJs must be appointed pursuant to the Appointments Clause turns on whether SEC ALJs "exercis[e] significant authority pursuant to the laws of the United States." *Buckley*, 424 U.S. at 126.[7] This Court has not had occasion to articulate the precise scope of that constitutional precondition. But a centuries-old understanding of the term "Officers of the United States" yields a rule fully consistent with the Appointments Clause's purpose and this Court's cases: An individual wields "significant authority" only if she holds an office that has been "delegat[ed] by legal authority ... a portion of the sovereign powers of the federal government." 2007 OLC Op. 78; *see* Resp. Br. 15. And for the reasons explained below, that criterion is satisfied only if the individual has (i) the power to bind the government or third parties (ii) in her own name rather than in the name of a superior officer.

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[7] Petitioners suggest that any appointee whose position includes "'tenure, duration, continuing emolument, or continuous duties'" is a constitutional officer. Pet. Br. 18 (quoting *Auffmordt v. Hedden*, 137 U.S. 310, 327 (1890)). It is true that holding "a continuing position[]" in the federal government "established by law"—as SEC ALJs indisputably do, *see supra* at 4-5—is a necessary precondition for officer status. *See, e.g.*, *Freytag*, 501 U.S. at 881; *Germaine*, 99 U.S. at 511-12; *see also The Constitutional Separation of Powers Between the President and Congress*, 20 Op. O.L.C. 124, 139-42, 145-47 (1996). But as the Solicitor General explains, it is not sufficient. An official must *both* "wield significant authority" *and* "occupy a continuing office" to become an "Officer of the United States." Resp. Br. 17-18 n.3; *accord* 2007 OLC Op. 73-74.

SEC ALJs are not "Officers of the United States" because they can do neither of these things. An SEC ALJ has no authority to bind the government or alter the rights of third parties at all. And regardless, even if an SEC ALJ in theory had such authority, it could be exercised solely in the name of the Commission, not in the ALJ's own name. The decision below should be affirmed.

I. ONLY SOMEONE WHO HAS BEEN LAWFULLY DELEGATED AUTHORITY TO BIND THE GOVERNMENT OR THIRD PARTIES IN HER OWN NAME CAN BE AN "OFFICER" UNDER THE APPOINTMENTS CLAUSE

As the Solicitor General agrees, an individual appointed to a continuing, statutorily created position in the federal government exercises "significant authority pursuant to the laws of the United States," *Buckley*, 424 U.S. at 126, and is therefore a constitutional officer, only if she has been delegated power to "exercise a portion of the sovereign authority of the United States." Resp. Br. 15. Such sovereign authority primarily consists of the power to "bin[d] the government or third parties for the benefit of the public, such as by administering, executing, or authoritatively interpreting the laws." 2007 OLC Op. 77; *see* Resp. Br. 15.[8] And even appointees who have

[8] "Delegated sovereign authority also includes other activities of the Executive Branch concerning the public that ... have long been understood to be sovereign functions, particularly the authority to represent the United States to foreign nations or to command military force on behalf of the government." 2007

such authority are not constitutional officers unless they have authority to exercise it in their own name rather than as a mere agent of a superior officer.

A. Only Persons Who Have Been Lawfully Delegated Authority To Bind The Government Or Third Parties Can Be Constitutional Officers

1. a. It has long been understood—and at least the Solicitor General does not dispute, Resp. Br. 15—that a constitutional officer is an individual "invested with some portion of the sovereign functions of government, to be exercised by him for the benefit of the public." Floyd R. Mechem, *A Treatise on the Law of Public Offices and Officers* § 1, at 1-2 (1890). As Mechem's treatise explained, "[r]eflecting the understanding from the first hundred years of American law, including pre-Founding English law," 2007 OLC Op. 84, the "delegation ... of some of the sovereign functions of government" is the "most important characteristic which distinguishes an office," and "[u]nless the powers conferred are of this nature, the individual is not a public officer," Mechem, *supra*, § 4, at 5; *accord* 2007 OLC Op. 77; *Office—Compensation*, 22 Op. Att'y Gen. 184, 187 (1898); *Appointment—Holding of Two Offices—Commissioner of Labor*, 26 Op. Att'y Gen. 247, 249 (1907).

This Court has explained, albeit in a somewhat different context, what it means to exercise a portion

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OLC Op. 77. Those other types of sovereign authority are not implicated here.

of the sovereign powers of the United States—*viz.*, to take action that "alter[s] the legal rights, duties and relations of persons," whether private parties or government actors. *I.N.S. v. Chadha*, 462 U.S. 919, 952 (1983); *see also* The Federalist No. 64, at 436 (Jay) (referring to the Constitution's allocation of "power to do" each "act of sovereignty by which the citizens are to be bound and affected"). The question is *not* whether the person can or does exercise functions that can be considered important—the fact that countless federal employees have "substantial practical authority" does not make them subject to the Appointments Clause. 2007 OLC Op. 98. Rather, the understanding since the Nation's early years has been that the *sine qua non* of officer status is the lawfully delegated authority to exercise "*legal* power" and "bind[] the government or third parties for the benefit of the public." *Id.* at 77, 98 (quotation omitted).

Acts that bind the government include filing enforcement actions in court or before an administrative body, making litigation decisions that bind the United States, and issuing binding interpretations of the law. Acts that bind private parties include issuing regulations that carry the force of law and entering final decisions in adjudications (which often also bind the government). Individuals holding continuing federal positions who exercise such sovereign authorities must be appointed pursuant to the Appointments Clause.

By contrast, "a person whose acts have no authority and power of a public act or law absent the subsequent sanction of an officer or the legisla-

ture"—for example, a person exercising "advisory" or "investigative" functions—is not an "Officer of the United States" but an employee. *Id.* at 95, 98 (quotation omitted). Thus, persons serving on an investigatory commission with the power (for example) to issue subpoenas, administer oaths, and examine witnesses but no authority to act on their findings or recommendations are not "Officers of the United States." *See infra* at 39-42.

b. This understanding of the meaning of a public "office" or "officer" is reflected in commentary from knowledgeable observers beginning before the Founding and continuing through the Nation's first Century.

The Continental Congress, for example, understood officers in England to be "persons holding sovereign authority delegated from the King that enabled them in conducting the affairs of government to affect the people 'against [their] will, and without [their] leave.'" 2007 OLC Op. 82 (quoting *King v. Burnell*, Carth. 478, 478 (K.B. 1700)).

Similarly, in 1822, the Supreme Judicial Court of Maine—in providing "the fullest early explication" of the term "Officer of the United States," *id.* at 83—explained that "[t]here is a manifest difference between an office, and an employment under the government," *Opinion of the Justices*, 3 Greenl. (Me.) 481, 482 (1822). An office "implies a delegation of a portion of the sovereign power to, and possession of it by the person filling the office," that "in its effects[,] ... will bind the rights of others." *Id.* Mere employment, in contrast, characterizes appointees who are "agent[s] act[ing] only on behalf of [their]

principal"—i.e., a superior officer—whose "sanction is generally considered as necessary to give the acts performed the authority and power of a public act." *Id.*

Surveying these and other materials, the Judiciary Committee of the House of Representatives in 1899 similarly concluded that an "office" requires a delegation of sovereign authority, which "involves necessarily the power to (1) legislate, or (2) execute law, or (3) hear and determine judicially questions submitted," 1 Asher C. Hinds, *Hinds' Precedents of the House of Representatives* 604, 607 (1907) ("Hinds")—i.e., the power to "bind the Government or do any act affecting the rights of a single individual citizen," *id.* at 610. Thus, the Committee concluded, membership on "a commission created by law to investigate and report, but having no legislative, judicial, or executive powers," did not constitute an "office." *Id.* at 604.

Likewise, the Executive Branch's longstanding view has been that an "Officer of the United States" is someone holding a continuing position created by federal law who has authority to "bind[] the government or third parties for the benefit of the public," 2007 OLC Op. 77, whereas a mere employee is "a person whose acts have no authority and power of a public act or law absent the subsequent sanction of an officer or the legislature," *id.* at 95 (quotation omitted); *see also Constitutionality of Proposed Regulations of Joint Committee on Printing*, 8 Op. O.L.C. 42, 48 (1984) (while the "administration and enforcement" of the law must be performed by constitutional officers, "investigative and informative" func-

tions need not be); *Common Legislative Encroachments on Executive Branch Authority*, 13 Op. O.L.C. 248, 249 (1989) (person occupying position that is merely "advisory," "investigative," or "informative" does not qualify as an officer).

2. This Court's more recent cases have stated that a constitutional officer has the power to exercise "significant authority pursuant to the laws of the United States." *Buckley*, 424 U.S. at 126; *see Freytag*, 501 U.S. at 881; *Edmond*, 520 U.S. at 663; *Free Enter. Fund*, 561 U.S. at 486. The Court has not had occasion to more concretely articulate the governing standard, but as the Office of Legal Counsel has explained, "the phrase 'significant authority pursuant to the laws of the United States'" should be understood as a "shorthand for the full historical understanding of the essential elements of a public office." 2007 OLC Op. 87. And this Court's cases from the beginning have labeled "officers" only those holding a continuing position in the federal government who are, at a minimum, authorized to bind the government or alter the rights of private parties.

a. This Court's recent cases reflect this understanding. The heads of the Federal Election Commission at issue in *Buckley* were authorized to "administer and enforce" federal legislation, and their "enforcement power [was] both direct and wide ranging." 424 U.S. at 111. They therefore possessed power both to bind the United States and to alter private parties' rights. And the members of the Public Company Accounting Oversight Board in *Free Enterprise Fund* were "charged with enforcing" various securities laws and standards, and were authorized

to issue regulations that carry the force of law. 561 U.S. at 485.

The Tax Court special trial judges and Court of Criminal Appeals military judges this Court considered in *Freytag* and *Edmond* possessed similar authorities to bind the government and alter third-party rights. Court of Criminal Appeals judges, for example, review *de novo* the most serious court-martial judgments, *Edmond*, 520 U.S. at 662, and review of their decisions is limited, particularly as to factual findings, *id.* at 664-65. Moreover, Court of Criminal Appeals judges have authority to "render a final decision on behalf of the United States," subject to review by superior executive officers. *Id.* at 665. Tax Court special trial judges also have the power, among other things, to enter final decisions in some cases. *Freytag*, 501 U.S. at 882, 891; *see infra* at 36.

This Court's modern cases, in short, have never held to be a constitutional officer anyone lacking authority to bind the government or alter the legal rights of private parties.

b. The same is true of this Court's earlier cases. As the Solicitor General correctly explains, many of those cases concerned "whether Congress *intended* to treat a position it had created by statute as an 'office,' not whether the functions of the position were so significant that the Constitution *required* that the position be held by an officer" of the United States. Resp. Br. 24. Therefore not all of those cases provide particularly helpful guidance about the type of significant authority this Court has deemed necessary for *constitutional* officer status. *See id.*

Even so, the positions that this Court's earlier cases called "offices" were delegated power to bind the government or alter private rights. *See, e.g., Ex parte Siebold*, 100 U.S. 371, 380 (1880) (federal marshals had authority, among other things, to "keep the peace and protect [election] supervisors in the discharge of their duties," "prevent fraudulent registration and voting," and "immediately to arrest any person who commits, or attempts to commit, ... any offence against the laws of the United States"); *id.* at 379-80 (election supervisors authorized, among other things, "to cause such names to be registered as they may think proper to be so marked ... and for purposes of identification to affix their signatures to each page of the original list," "to challenge any vote the legality of which they may doubt," and to "require[]" deputy marshals to perform certain duties, Act of Feb. 28, 1871, 16 Stat. 433, 436[9]); *United States v. Allred*, 155 U.S. 591, 594-95 (1895) (federal circuit court commissioners, among other things, "issue[d] warrants," "cause[d] the offenders to be arrested and imprisoned, or bailed, for trial," and "institute[d] prosecutions under the laws relating to crimes against the elective franchise and civil rights of citizens"); *Rice v. Ames*, 180 U.S. 371, 374 (1901) (extradition commissioners, like other commissioners, had power to issue arrest warrants and imprison offenders); *Go-Bart Importing Co. v. United States*, 282

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[9] *See also United States v. Gitma*, 25 F. Cas. 1323, 1323 (C.C.E.D. Va. 1879) (relevant Act "provides that *'when required' to do so by the supervisors* it shall be the duty of deputy marshals to 'attend the polls' in their districts or precincts" (emphasis added)).

U.S. 344, 353 n.2 (1931) (federal district court commissioners had authority, among other things, to "arrest and imprison" defendants, to "issue warrants for" fugitives, to "issue search warrants," and to "institute prosecutions under laws relating to the elective franchise and civil rights"); *Myers v. United States*, 272 U.S. 52, 158 (1926) (postmaster first-class assumed to be an officer was authorized by statute to, among other things, resolve certain disputes, Act of June 8, 1872, Ch. 335, 17 Stat. 283, 307, issue money orders, *id.* at 297-300, and "affix his signature to the certificate of sufficiency of guarantors or sureties," *id.* at 313); *Myers*, 272 U.S. at 159 (U.S. Attorney, who can make litigation decisions on behalf of the United States, is an "inferior officer"); *Ex parte Hennen*, 38 U.S. (13 Pet.) 230 (1839) (district court clerk described as an "inferior officer" was required to provide a bond to the United States in case of a suit brought against him, *see* Act of Sept. 24, 1789, Ch. 20, 1 Stat. 73, 76, making clear that he exercised authority that affected individual rights).

This Court's cases are thus fully consistent with the traditional understanding that federal appointees are "Officers of the United States," requiring appointment in conformity with the Appointments Clause, only if (among other things) they have authority to bind the government or alter the rights of private parties.

B. Appointees Who Have Authority To Bind The Government Or Alter Private-Party Rights Only As Agents Of A Superior Officer Are Not Themselves Constitutional Officers

Although the authority to bind the government or private parties is a necessary precondition of constitutional officer status—and the lack of it here resolves this case, *see infra* Part II—it is not sufficient. Longstanding practice, Executive Branch understanding, and this Court's precedents all confirm that even an appointee to a continuing position in the federal government who has the de facto power to bind the government or alter private rights is *not* a constitutional officer if that power cannot be exercised in the appointee's own name, but only in the name of a superior who is a constitutional officer.

The First Congress, for example, established various deputy positions and vested appointment authority for those positions in the deputies' principals even though the principals were not department heads. Specifically, the First Congress authorized marshals, collectors, and surveyors—none of whom was the head of a department—to appoint their own deputies to assist them in their duties. 1 Stat. 73, 87; Act of Aug. 4, 1790, Ch. 35, 1 Stat. 145, 155; *see also* Jennifer L. Mascott, *Who Are "Officers of the United States"?*, 70 Stan. L. Rev. 443, 525-26 & nn.491-96 (2018) (explaining why the appointing officers were not department heads).

The fact that the First Congress chose a method of appointment for these deputies that the Appointments Clause does not specify demonstrates that it

did not consider them to be constitutional officers. Yet these deputies had substantial authority to impact the rights of nongovernmental parties. To take one example, deputy marshals assisted their principal in maintaining custody over federal prisoners. 1 Stat. 73, 88; *see United States v. Mundell*, 6 Call. 245, 246, 248-49 (C.C.D. Va. 1795). To take another, collectors could authorize their deputies to grant permits for ships to unload imported goods. 1 Stat. 152, 155. The First Congress thus understood that deputies who acted only as agents of their superiors (rather than under authority delegated to their own office) need not be constitutional officers.

This Court reached the same conclusion in *Germaine*, where it held that a civil surgeon appointed by the commissioner of pensions was not a constitutional officer because "[h]e [wa]s but an agent of the commissioner." 99 U.S. at 512; *accord Auffmordt*, 137 U.S. at 328. And in *Steele v. United States*, 267 U.S. 505 (1925), the Court concluded that deputy marshals were "not in the constitutional sense ... officer[s] of the United States" even though they, along with the marshal, "are the persons chiefly charged with the enforcement of the peace of the United States, as that is embraced in the enforcement of federal law," *id.* at 508, and even though deputy marshals are "called upon to exercise great responsibility and discretion in the service of" their duties, *id.*

Executive Branch opinions have long reflected the same view. In 1871, for example, the Attorney General explained that Congress provided non-Article II selection methods for positions such as

deputy marshal because "the office was substantially in the principal." *Civil-Service Commission*, 13 Op. Att'y Gen. 516, 521 (1871). These deputies, in other words, were only the "representatives" of a principal who was ultimately "responsible for their conduct." *Id.* Deputy district court clerks, in contrast, *were* officers because they were not only granted authority to "do every act which [their] principal[s] might do," but could do them in their "own name as deputy." *Deputy Clerks of United States District Courts—Premium on Official Bonds*, 29 Op. Att'y Gen. 593, 597 (1912). Thus, as the Office of Legal Counsel has more recently explained, an "agent" who "acts only on behalf of his principal" and has no power in his own office is merely an employee. 2007 OLC Op. 98 (quotation omitted); *cf. The Constitutional Separation of Powers Between the President and Congress*, 20 Op. O.L.C. at 144 n.57 ("That an employee may not exercise *independent* discretion does not, of course, mean that his or her duties may not encompass responsibilities requiring the exercise of judgment and discretion under the ultimate control and supervision of an officer."). This long-established rule "preserve[s] political accountability," *Edmond*, 520 U.S. at 663, because the principal will be held accountable for the agent's acts in the principal's name.

C. This Court Should Not Expand The Meaning Of The Term "Officers Of The United States" Beyond Its Historically Understood Limits

Petitioners (and the Solicitor General) seek to expand the category of constitutional officers dra-

matically beyond its historical limits, contending that this category is "expansive" and "sweeping." Pet. Br. 16. Although petitioners never clarify exactly how "significant authority" should be measured, they suggest that the category includes any authority that can colloquially be described as important, significant, or non-ministerial. *See, e.g.*, Pet. Br. 21-23. And they rely heavily on this Court's statement in *Freytag* that characterized as "significant" the authority of special trial judges to "take testimony, conduct trials, rule on the admissibility of evidence, and ... enforce compliance with discovery orders." 501 U.S. at 881-82. Petitioners contend that any federal appointee who exercises similar hearing-related functions (including SEC ALJs) must be a constitutional officer. Pet. Br. 23; *see* Resp. Br. 21.

It is true that language in *Freytag* could be construed broadly to require that anyone who exercises authority that could be deemed "significant" in a colloquial sense—such as presiding over a hearing—is an officer even if she has no authority to bind the government or alter private-party rights, let alone to do so in the name of her own office. But *Freytag* never considered, let alone purported to alter, the longstanding traditional view of the scope of the Appointments Clause. *Cf.* 2007 OLC Op. 86 (the reference to "significant authority" in *Buckley* and subsequent cases "does vary somewhat from the well-established historical formulation, but nothing in the Court's opinion suggests any intention to break with the longstanding understanding of a public office or fashion a new term of art" (citation omitted)). And there is no need to adopt petitioners' and the Solici-

tor General's ahistorical and overly broad construction to support the holding in *Freytag*, which is fully consistent with the traditional understanding.

Petitioners' reading of *Freytag*, moreover, would have significant negative practical consequences (including calling into question the constitutionality of more than a century's worth of presidential and congressional investigative commissions), would not materially advance the purpose of the Appointments Clause, and would be difficult for the political branches to administer.

1. The traditional rule fully supports the Court's holding in *Freytag* because the special trial judges at issue in that case undoubtedly had authority to bind the government and private parties, in at least two respects.

First, they could enter binding final judgments in their own name in some circumstances, 501 U.S. at 882, which suffices to establish their officer status. It is true that the Court's opinion stated that the authority to issue final judgments "would" confirm special trial judges' officer status "[e]ven if" their hearing-related duties described above "were not as significant" as the Court believed. *Id.* Even so, special trial judges' ability to enter final judgments fully supported the Court's holding, and it was therefore unnecessary to the Court's holding to consider the constitutional status of other appointees who do not possess such authority.

Second, the hearing-related functions of special trial judges that this Court collectively labeled "significant" included the power to bind the government

and private parties by "enforc[ing] compliance with discovery orders." *Id.* at 881-82. As the SEC explained below, special trial judges had "power to enforce compliance with discovery orders" because they had authority to punish contempt. SEC C.A. En Banc Br. 31 (quotation omitted).[10] And the "power of contempt is a hallmark of an adjudicative official's status as a constitutional officer," *id.* at 33, precisely because it is a power to bind the government and private parties.

The Solicitor General acknowledges this contempt power but argues that what the Court in *Freytag* found important was that special trial judges could enforce discovery orders, and not "the particular type" of enforcement power special trial judges possessed. Resp. Br. 21 n.4 (quotation omitted). But it is not apparent what authority other than the power to punish contempt allowed special trial judges to "enforce compliance with discovery orders," 501 U.S. at 882, as the Commission acknowledged below, SEC C.A. En Banc Br. 31. If special trial judges lacked contempt power, they would have been "dependent upon [a] court for enforcement" of a subpoena or other order. *Proposed Legislation to Grant*

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[10] The Court in *Freytag* noted the Tax Court's contempt power. *See* 501 U.S. at 891 (citing 26 U.S.C. § 7456(c)). The Tax Court has delegated to special trial judges various hearing-related powers, including the power to issue subpoenas, administer oaths, examine witness, and rule on the admissibility of evidence, and has also delegated "such further and incidental authority ... as may be necessary for the conduct of trials and other proceedings." Tax Ct. R. 181 (1990). Congress labeled the contempt power an "incidental" authority in the statute granting that authority to the Tax Court. 26 U.S.C. § 7456(c).

Additional Power to The President's Commission on Organized Crime, 7 Op. O.L.C. 128, 130 (1983).

Admittedly, the other special trial judge functions that this Court mentioned—i.e., the power to "take testimony, conduct trials, [and] rule on the admissibility of evidence," *Freytag*, 501 U.S. at 881-82—are unconnected to the power to punish contempt or otherwise bind the government or alter private-party rights. But *Freytag* did not consider whether—let alone conclude that—any such authority alone would have been enough to establish officer status. Certainly, the mere mention of such functions among others that *do* empower special trial judges to bind parties should not be read to overcome the centuries-old understanding that the power to bind the government or private parties is a necessary condition for constitutional officer status.[11]

2. Adopting petitioners' standard would also have significant adverse practical consequences.

For one thing, a rule that classifies anyone who performs "important," "significant," or "nonministerial" tasks as an officer could result in subjecting, for example, every government attorney, investigator, and law-enforcement officer to the Ap-

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[11] Special trial judges arguably also have power to bind the government in another respect: the Tax Court must accept their findings of fact unless "clearly erroneous." *See* Tax Ct. R. 183(d) ("the findings of fact recommended by the Special Trial Judge shall be presumed to be correct"); *see also Stone v. Comm'r*, 865 F.2d 342, 347 (D.C. Cir. 1989) (interpreting same language in prior version of Tax Court rules to provide for clearly erroneous standard of review).

pointments Clause. Petitioners' rule could cast doubt on the constitutionality of the method of appointment of many thousands of civil servants.

Adopting petitioners' and the Solicitor General's reading of *Freytag*, moreover, would call into significant doubt the validity of a more-than-a-century-old, unbroken congressional practice of establishing commissions that include members not appointed under the Appointments Clause—including members of Congress—and that have historically been granted authority to exercise hearing-related powers akin to those possessed by special trial judges (and SEC ALJs, *see infra* at 48-50), but *not* the power to punish contempt. For example, such commissions typically possess the powers incident to investigation, e.g., to issue subpoenas, administer oaths, collect documents, and call and examine witnesses. *See, e.g.*, *Proposed Legislation to Grant Additional Power to The President's Commission on Organized Crime*, 7 Op. O.L.C. at 130 & n.7 (list of many such commissions); *Proposed Commission on Deregulation of International Ocean Shipping*, 7 Op. O.L.C. 202, 202 (1983) (discussing congressional commissions). If such authorities sufficed to establish officer status, then these commissions would be irredeemably unconstitutional: even if they could otherwise be staffed with properly appointed constitutional officers, members of Congress would absolutely be precluded from serving on them by the Incompatibility Clause, which prohibits Senators and Representatives from being "appointed to any civil Office under the Authority of the United States." U.S. Const. art. I, § 6, cl. 2.

Yet both Congress and the Executive have for more than a century consistently concluded that such committees pose no Appointments Clause or Incompatibility Clause problem precisely because, despite the hearing-related powers they (like special trial judges) possess, such commissions can investigate, make findings, and make recommendations, but (unlike special trial judges) they cannot enforce those findings or recommendations to bind the government or private parties.

Thus, for example, the House Judiciary Committee's 1899 report described earlier, after "extensively survey[ing] the definition of an 'office,'" 2007 OLC Op. 85, and concluding that investigation and reporting are not officer functions, *see supra* at 27, applied its analysis to certain commissions that Congress had recently created, considering whether the Incompatibility Clause precluded members of Congress from serving on them, Hinds at 611. The Committee concluded that commission membership was not an office, even when the commission was empowered to, for example, administer oaths, issue subpoenas, and collect documents and examine witnesses. *See, e.g.*, An Act of 1898, Ch. 447, 30 Stat. 445; An Act of 1898, Ch. 466, 30 Stat. 476.

The Office of Legal Counsel similarly has concluded that investigative commission members are not constitutional officers despite subpoena and other related powers when they "possess no enforcement authority or power to bind the Government." *Proposed Commission on Deregulation of International Ocean Shipping*, 7 Op. O.L.C. at 202; *see also id.* at 203 (noting relevant commission's power to is-

sue subpoenas and examine witnesses); *see also Constitutionality of Proposed Regulations of Joint Committee on Printing*, 8 Op. O.L.C. at 48 (non-officers may exercise "investigative and informative powers of the type generally delegated to congressional committees"). And that Office has specifically concluded that non-officers can issue subpoenas and administer oaths, and explained that the subpoena power in particular "has not been viewed as the exercise of a coercive power": the issuing agent is "dependent upon the courts for enforcement" of the subpoena by punishing contempt, and no "matter what the issuing agent finds out, it cannot, in the absence of any other power, use the information to *do* anything, such as enact or execute a law, adjudicate a dispute, or otherwise take any affirmative action which will affect an individual's rights." *Proposed Legislation to Grant Additional Power to The President's Commission on Organized Crime*, 7 Op. O.L.C. at 130 (quotation omitted). The same is true of other hearing-related powers, such as the power to call witnesses, admit evidence, and administer oaths—if those authorities do not include the power to use the information collected "to *do* anything" that binds the government or private parties, it has uniformly been understood that those powers need not be wielded by officers.[12]

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[12] The Office of Legal Counsel has also made clear that such commissions *would* meet the other requirements of a constitutional office—e.g., tenure and continuing duties—if the commission *could* take binding action based on its findings. *See, e.g., Constitutionality of the Ronald Reagan Centennial Commission Act of 2009*, 2009 WL 2810453, at *2 & n.6 (O.L.C.

Petitioners' argument that hearing-related powers similar to those typically possessed by investigative commissions establish officer status cannot be reconciled with this joint Legislative and Executive Branch practice and understanding.[13]

3. Petitioners' standard would also not materially advance the purpose of the Appointments Clause, namely, "to preserve political accountability relative to important Government assignments." *Edmond*, 520 U.S. at 663.

The constrained historical understanding of the attributes of a constitutional office appropriately ensures that the President (directly or through a direct appointee) will be accountable for the acts of those who themselves bind the government or private parties, because the President or his direct appointee is responsible for appointing the actor who exercised that authority. By contrast, when "a person['s] ...

Apr. 21, 2009) ("members of an unpaid commission ... [can] hold offices in the constitutional sense" (citing prior opinions)).

[13] Petitioners' sweeping construction could also have unpredictable implications for the application of other constitutional provisions that turn on "Officer" status, such as the Impeachment Clause and the Foreign Emoluments Clause, both of which only apply to constitutional officers. U.S. Const. art. I, § 9, cl. 8; *id.* art. II, § 4; *see, e.g.*, *Application of the Emoluments Clause to a Member of the President's Council on Bioethics*, 29 Op. O.L.C. 55, 70-71 & n.8 (2005) (describing and approving the traditional view of the Department of Justice that "Office of Profit or Trust under [the United States]" in the Foreign Emoluments Clause is synonymous with "Officer of the United States" in the Appointments Clause, thereby limiting the number of persons in the federal workplace who are subject to the complex restrictions of the former).

acts have no authority ... absent the subsequent sanction of an officer," 2007 OLC Op. 95 (quotation omitted), the officer who grants the "subsequent sanction" (and the President or the President's direct subordinate who appointed that officer) will be, and should be, held *directly* accountable for the decision. Likewise, when an employee acts solely in the name of a superior officer, that superior will be blamed or praised for acts done in his name—regardless of the method by which the employee was hired—and the President is accountable for the superior's appointment. *Cf. Andrade v. Regnery*, 824 F.2d 1253, 1257 (D.C. Cir. 1987) (such delegation "does not offend the Appointments Clause so long as the duly appointed official has final authority over the implementation of the governmental action").

4. Finally, construing "Officer of the United States" to turn on the authority to bind the government or alter private rights in the officer's own name—rather than on an amorphous standard based on a subjective assessment of the perceived importance or significance of the appointee's authority —would provide an administrable rule for Congress and the Executive Branch to determine which positions require compliance with the Appointments Clause and other constitutional provisions applicable to officers. Adopting petitioners' vague standard would complicate the political branches' efforts to comply not only with the Appointments Clause but also other constitutional provisions (such as the Foreign Emoluments Clause, *see supra* at 42 n.13) that turn on officer status.

II. SEC ADMINISTRATIVE LAW JUDGES ARE NOT "OFFICERS OF THE UNITED STATES" FOR PURPOSES OF THE APPOINTMENTS CLAUSE

Under the foregoing principles, SEC ALJs are not constitutional officers subject to the Appointments Clause.

A. SEC ALJs Are Not Constitutional "Officers" Because They Cannot Bind The Government Or Alter The Rights Of Private Parties In Their Own Name

1. *SEC ALJs Have No Authority To Bind The Government Or Private Parties*

a. SEC ALJs have no authority to bind the Commission in any respect. Congress provided that "the Commission shall retain a discretionary right to review the action of any [delegee, including an] administrative law judge, ... upon its own initiative or upon petition of a party to or intervenor in such action." 15 U.S.C. § 78d-1(b). Consistent with that directive, the Commission can revisit *de novo* any finding of fact or determination of law made by an ALJ, *see id.*, and "ultimately controls the record for review and decides what is in the record," Pet. App. 91a; *see* 17 C.F.R. §§ 201.411(a), 201.452. Thus, unlike (for example) the Court of Criminal Appeals military judges in *Edmond*, whose factual findings could be revised only when not supported by substantial evidence, 520 U.S. at 665, every decision an SEC ALJ makes can be revised fully by the Commission, so the Commission "is in no way bound by the decision"

of the ALJ, *Attorney General's Manual on the Administrative Procedure Act* 83 (1947).

Petitioners and the Solicitor General believe it important that, as a factual matter, the Commission often decides to defer to an ALJ's credibility determinations, Pet. Br. 24; Resp. Br. 36-37, but that is irrelevant: it is undisputed that the Commission has no legal obligation to defer to ALJ credibility determinations, and thus that ALJs have no authority to bind the Commission, *see* Pet. App. 92a-93a n.117, which is what matters for officer status. If and when the Commission *chooses* to defer to the ALJ, the Commission itself is accountable for that decision.

b. SEC ALJs also lack authority to make final decisions that are binding on private parties (or the Commission). They are authorized only to issue initial decisions, 17 C.F.R. § 201.360, which have no force of their own—no party's rights are affected until *the Commission* issues a final decision.

The Commission can issue a final decision after conducting plenary review, either when a petition for review is filed, *id.* § 201.411(b), or when the Commission elects to review the ALJ's decision on its own initiative, *id.* § 201.411(c). If the Commission decides not to conduct plenary review, an ALJ initial decision cannot take effect until the Commission issues a finality order. *Id.* § 201.360(d)(2).[14] Even in the case of a default, the ALJ must issue an initial

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[14] Petitioners err in describing finality orders as "non-discretionary." Pet. Br. 33. The Commission issues a finality order only if it has decided not to exercise its discretion to conduct plenary review. 17 C.F.R. § 201.360(d)(1).

decision, which is then subject to review through one of the mechanisms just described. *See supra* at 11.

Both petitioners and the Solicitor General emphasize that the Commission does not actually engage in plenary review in most cases. Pet. Br. 32-33; Resp. Br. 22. That is true, *see supra* at 11 n.6, but beside the point. The relevant question, as petitioners admit, "'is simply whether a position possesses delegated sovereign authority to act in the first instance, whether or not that act may be subject to direction or review by superior officers.'" Pet. Br. 30-31 (quoting 2007 OLC Op. 75). SEC ALJs have *not* been delegated "sovereign authority to act in the first instance" because their initial decisions do not themselves alter the legal rights of individuals (or bind the government). Those initial decisions "have no authority and power of a public act or law absent the subsequent sanction of an officer," 2007 OLC Op. 95 (quotation omitted)—i.e., the sanction of the Commission either after plenary review or through the issuance of a finality order.

The lack of any delegated power to issue binding decisions distinguishes SEC ALJs from the special trial judges in *Freytag*. *See supra* at 36. It also distinguishes SEC ALJs from judges on the Court of Criminal Appeals in *Edmond*. Those judges had authority to enter binding final decisions in their own name, subject to review (but not *de novo* review) by superior executive officers. *Edmond*, 520 U.S. at 665; *see also* U.S. *Edmond* Br., 1997 WL 33018, at *25 (Court of Criminal Appeals "authorized by statute to issue final decisions that are reviewable under a deferential standard"). As petitioners and the So-

licitor General correctly note, Pet. Br. 29; Resp. Br. 35, the fact that the Court of Criminal Appeals' final decisions were reviewable by a superior executive officer was, in part, what made those judges inferior rather than principal officers. *Edmond*, 520 U.S. at 665. But the fact that they could issue final decisions that became effective absent subsequent sanction by a superior officer is at least one reason why those judges were constitutional officers in the first place.

c. The Solicitor General recognizes that under Commission regulations, even when the Commission decides not to conduct plenary review, an ALJ's initial decision has no force absent a Commission finality order. Resp. Br. 35. He contends, however, that "the ALJ's decision is still the Commission's final decision by operation of [§ 78d-1(c)]," *id.*, which provides that if the Commission declines to exercise review, or if no review is sought, "then the action of [the delegee, including an] administrative law judge, ... shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission," 15 U.S.C. § 78d-1(c).

That is incorrect. Subsection (c) does not come into play at all unless the ALJ exercises a function delegated under subsection (a). But the Commission has not delegated ALJs the authority to enter a decision that can have effect without the Commission's affirmative sanction through a finality order. *See supra* at 10-11. Thus, subsection (c)'s "deemed" provision does not apply to ALJ initial decisions.

Moreover, even if the Solicitor General's reading of § 78d-1(c) were correct, it would only confirm that

SEC ALJs are not constitutional officers. After all, § 78d-1(c) deems an ALJ's initial decision to be the decision *of the Commission*, not the ALJ. In other words, even if ALJs had de facto authority to alter a party's rights, they could only do so in the name *of the Commission*.

In this respect, ALJs are akin to the non-officer deputies that Congress established as early as 1789—"agent[s]" who "act[] only on behalf of [their] principal," i.e., the Commission. 2007 OLC Op. 98 (quotation omitted). The fact that Congress did not delegate SEC ALJs any power to issue decisions in their own name shows that they are not officers but "representatives" of the Commission, which is ultimately "responsible for their conduct," *Civil-Service Commission*, 13 Op. Att'y Gen. at 521, and which can and will be held accountable for that conduct, consistent with the Appointments Clause's purpose, *see supra* at 1-2.

d. Petitioners and the Solicitor General also rely heavily on other functions SEC ALJs may perform when presiding over hearings. They note that SEC ALJs may, for example, administer oaths, issue subpoenas, hold hearings, take testimony, and admit evidence. Pet. Br. 23; Resp. Br. 21. But as explained earlier, it has long been understood that non-officers can exercise such hearing-related powers—powers routinely possessed by bodies serving investigative functions whose members are not constitutional officers. *See supra* at 39-42.

Petitioners and the Solicitor General point to *Freytag*'s statement that the power to "take testimony, conduct trials, rule on the admissibility of evi-

dence, and ... enforce compliance with discovery orders," 501 U.S. at 881-82, is "significant." But SEC ALJs do *not* have the power to "enforce" discovery or any other orders in any way relevant to the Appointments Clause, because they "have no authority to punish disobedience of discovery orders or other orders with contempt sanctions of fine or imprisonment." Pet. App. 7a; *see supra* at 9. Indeed, as the Commission explained, SEC ALJs are even "powerless to enforce their subpoenas. The Commission itself would need to seek an order from a federal district court to compel compliance." Pet. App. 94a n.120 (citing 15 U.S.C. § 78u(c)). SEC ALJs only have power to deal with "contemptuous conduct" "during a proceeding"—they can exclude the offending party from the hearing room or prevent him from representing others in the proceedings. 17 C.F.R. § 201.180(a). That limited authority is subject to immediate review by the Commission, *id.* § 201.180(a)(2), and if not reviewed is deemed an action of the Commission, 15 U.S.C. § 78d-1(c), so it cannot create officer status. *See supra* at 47-48. And even if done in the ALJ's own name, this power—along with SEC ALJs' other hearing-related powers, such as the power to admit evidence—is an authority anyone performing an investigative function would have.

Such authority, by itself, does not establish a constitutional office, *see supra* at 39-42, because its exercise does not by itself "alter[] the legal rights, duties and relations of persons." *Chadha*, 462 U.S. at 952. To be sure, an officer who *does* have authority to bind the government or private parties may use

powers inherent in conducting a hearing or investigation to find the facts necessary to determining the parties' legal rights. But if "no matter what [a federal actor] finds out" at the conclusion of the hearing or investigation, the actor cannot "use the information to *do* anything, such as enact or execute a law, adjudicate a dispute, or otherwise take any affirmative action which will affect an individual's rights," *Proposed Legislation to Grant Additional Power to The President's Commission on Organized Crime*, 7 Op. O.L.C. at 130 (quotation omitted), she is not an officer.

To be sure, an appointee's role in "shaping the record" through such functions, Pet. Br. 24; Resp. Br. 20, 24, *could* suggest officer status if the appointee's evidentiary rulings and other acts actually "shaped the record" in a manner binding on the agency.[15] But as explained above, no SEC ALJ's evidentiary

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[15] Contrary to petitioners' suggestion, magistrate judges are not officers based solely on their ability to "shape the evidentiary record" in a federal court case. Pet. Br. 30. Magistrate judges are authorized to enter final judgments, 28 U.S.C. § 636(c)(1), and enter unreviewable orders, *Roell v. Withrow*, 538 U.S. 580, 585 (2003); 28 U.S.C. § 636(c)(3). They may also enforce those orders and others through the contempt power, and may summarily order imprisonment or a fine. 28 U.S.C. § 636(e). Magistrates can also issue arrest warrants, 18 U.S.C. § 3041; authorize criminal complaints, Fed. R. Crim. P. 3; order pre-trial detention, 18 U.S.C. §§ 3141(a), 3142(a)(4); detain material witnesses, 18 U.S.C. § 3144; try misdemeanor cases, 18 U.S.C. § 3401(a); and impose sentences for petty offenses without the parties' consent, 28 U.S.C. § 636(a)(4). Magistrate judges are therefore constitutional officers for reasons having nothing to do with their ability to "shape the evidentiary record."

ruling is binding on the Commission, which has plenary authority to determine and analyze the record—an authority the Commission exercised in this case. *See supra* at 12. SEC ALJs simply have no power to bind the government or private parties, let alone the power to do so in the ALJ's own name rather than that of the Commission. SEC ALJs therefore are not constitutional officers subject to the Appointments Clause.

2. *SEC ALJs Are Not Comparable To Article III Judges In Any Relevant Respect*

Petitioners and the Solicitor General also argue that SEC ALJs are constitutional officers because of a "parallel between ALJs and Article III judges." Resp. Br. 25; *see* Pet. Br. 18-20. Not so.

SEC ALJs preside over proceedings that "are adversarial in nature." *Butz*, 438 U.S. at 513. ALJs thus may do many things that Article III judges also do, including exercise the hearing-related functions described above. And ALJs are "functionally comparable" to judges in the sense that "the process of agency adjudication," like the process by which a court decides a case, is "structured so as to assure that the hearing examiner exercises his independent judgment on the evidence before him, free from pressures by the parties or other officials within the agency." *Id.*

Thus, ALJs' adjudicative functions render them sufficiently analogous to trial judges to afford ALJs absolute immunity for actions taken in presiding over agency hearings. *Id.* at 514. The similarities between agency adjudications and judicial proceed-

ings also warrant granting the States sovereign immunity in agency proceedings held before ALJs, *Fed. Mar. Comm'n v. S.C. State Ports Auth.*, 535 U.S. 743, 753-67 (2002), although the final decision in *Federal Maritime Commission* was rendered by the Commission, not an ALJ, *id.* at 750. But it does not follow that SEC ALJs must be "Officers of the United States" simply because district court judges are. SEC ALJs lack the crucial authorities that district courts possess—*viz.*, the authority to bind the government or private parties, for example by entering binding final judgments or punishing contempt. SEC ALJs thus are nothing like district court judges in any way that matters for Appointments Clause purposes.

It is certainly true, as the Solicitor General explains, Resp. Br. 27, that Congress in the APA sought to make ALJs "a special class of semi-independent subordinate hearing officers." *Ramspeck*, 345 U.S. at 132 (quotation omitted). Congress achieved this balance by giving ALJs "limited separation from their agencies with respect to 'their tenure and compensation,'" Pet. Br. 37 (quoting *Ramspeck*, 345 U.S. at 132 n.2), so that they would be able to maintain neutrality in evaluating evidence and formulating their initial decisions, *see supra* at 3-5. But as petitioners recognize, by keeping ALJs within the agency, Congress also ensured that hearing examiners would be "subordinate to their respective agencies" in "every ... significant respect" *other than* "tenure and compensation." Pet. Br. 37-38. Crucially, Congress did *not* seek to increase ALJ independence—and certainly not SEC

ALJ independence—by granting ALJs independent authority to bind the government or private parties. That is the authority that matters, and it is lacking here.

There is some irony, moreover, in petitioners' complaint that, despite the structural independence that Congress *has* provided ALJs, they are still not sufficiently "independent." Pet. Br. 38-40. If that is so, adopting petitioners' position would only make matters worse, since requiring appointment by a high-level political officer is itself a form of political control over the appointee. *Cf.* Barron & Kagan, *Chevron's Nondelegation Doctrine*, 2001 Sup. Ct. Rev. 201, 223 n.80 (2001) ("Presidents often have a good deal of actual control over independent agencies [despite for-cause removal restrictions] by virtue of their appointments and other powers."). Congress gave agencies like the Commission flexibility to enhance ALJs' structural independence beyond what the APA requires by authorizing them to delegate the power to hire ALJs to non-political employees—as the Commission had until recently done, *see supra* at 7—while at the same time reserving policymaking and decisionmaking authority (and thus accountability) to the Commission. The manner in which Congress achieved this balance is fully consistent with the Appointments Clause, and there is no reason to disturb it.

B. SEC ALJs' Employee Status Is Consistent With The Purpose Of The Appointments Clause

The Appointments Clause's accountability purpose is fully served by classifying SEC ALJs as em-

ployees rather than constitutional officers. Because "the Commission is not bound in any way by its ALJ[s'] decisions," "the blame for its unpopular decisions," as well as the praise for its good ones, "fall[s] squarely on the commissioners and, in turn, the president who appointed them." *Bandimere*, 844 F.3d at 1198 (McKay, J., dissenting). Indeed, because SEC ALJ decisions have no force without subsequent Commission action—and because those decisions in all events are issued in the name of the Commission, not the ALJ—it is "quite clear where the buck stops" in matters initially heard by an SEC ALJ. *Id.* Thus, "[s]o long as *the commissioners* have been validly appointed"—which no one disputes here—"the Appointments Clause is satisfied." *Id.* (emphasis added).

C. Congress Has Not Adopted The View That ALJs Are Constitutional "Officers Of The United States"

Finally, petitioners (but, notably, not the Solicitor General) also argue that "Congress provided, in both the securities laws and the APA, that ALJs are 'officers,'" a designation petitioners say "is all but dispositive of [SEC ALJs'] status under the Appointments Clause." Pet. Br. 12. Although congressional intent is "not dispositive of the constitutional question here," Resp. Br. 29, Congress has long made abundantly clear its view that ALJs are *not* constitutional officers but employees.

Petitioners correctly note that the APA originally described ALJs as "officers," and the securities laws refer to them as "officers of the Commission." *See* Pet. Br. 35-36. But that does not mean that

Congress understood SEC ALJs to be constitutional officers for purposes of the Appointments Clause. Petitioners cite *Germaine*, which concluded that the statutory term "Officer of the United States" there carried the same meaning as under the Appointments Clause. 99 U.S. at 510. Unlike in *Germaine*, however, Congress has never referred to ALJs as officers *of the United States*. And even if Congress had used that more specific term, this Court has held that the phrase "'officer of the United States,' when employed in the statutes of the United States, is to be taken usually to have the limited constitutional meaning," but can also "include others than those appointed by the President, heads of departments, and courts." *Steele*, 267 U.S. at 507. Congress's reference to ALJs as simple "officers" or "officers of the Commission" does not demonstrate an intent to create a constitutional office. *See also Lamar v. United States*, 240 U.S. 60, 65 (1916) ("words may be used in a statute in a different sense from that in which they are used in the Constitution"); *United States v. Hendee*, 124 U.S. 309, 313 (1888) (clerk was "officer" under compensation statute, even though he was "not, in the constitutional sense of the word, an officer of the United States").

In any event, any doubt about Congress's understanding was erased in 1966, when it restated and codified Title 5 of the U.S. Code "without substantive change." H.R. Rep. No. 89-901, at 1 (1965). Petitioners correctly explain that Congress in 1966 "*defined* 'officer' in the APA as 'an individual ... required by law to be appointed in the civil service by' 'the President,' 'a court of the United States,' or 'the

head of an Executive agency' or 'military department.'" Pet. Br. 36 (emphasis in original) (citing 5 U.S.C. § 2104(a)(1)); *see* Pub. L. No. 89-554, 80 Stat. 378, 408-09 (1966). What petitioners miss, however, is that Congress simultaneously deleted every reference to ALJs (then called "hearing examiners") as "officers," and replaced each such reference with "employee," *e.g.*, 80 Stat. 386-87, which is how these provisions read today, *e.g.*, 5 U.S.C. §§ 556, 557 (describing ALJ as "presiding employee"); *see also id.* § 2105(a) (defining "employee" to include individuals "appointed in the civil service by ... an individual who is an employee under this section"). The fact that Congress added definitions of "officer" and "employee" to Title 5 and at the same time made clear that ALJs were employees refutes petitioners' contention that Congress understood ALJs to be constitutional officers.[16]

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[16] Petitioners err in asserting that the APA's legislative history shows that Congress "understood that hearing examiners would be executive Officers." Pet. Br. 36. When formulating the APA, Congress considered a proposal "that the Judicial Conference appoint an officer to appoint and remove examiners," *Administrative Procedure Act: Legislative History, 79th Congress, 1944-46*, at 50, which raised concerns about possible "constitutional problems as to the appointing power," *id.*, given that "the Judicial Conference is a committee and not a court," *id.* at 42. The problem was not that *hearing examiners* had to be appointed in conformity with the Appointments Clause, but that a position assigned responsibility for appointing and removing hearing examiners for all agencies might have to be filled by a constitutional officer chosen under the Appointments Clause—which would not have occurred under the proposal that the Judicial Conference choose the appointing officer, because the Judicial Conference is not a court of law (or depart-

Petitioners also suggest in passing what appears to be a *statutory* argument: that by granting the "agency" authority to appoint ALJs, 5 U.S.C. § 3105, Congress intended that ALJs could be appointed only by agency *heads*, an obligation petitioners believe "the Commission has failed to discharge," Pet. Br. 3. Not so. Congress authorized the Commission to delegate "any of its functions to," among others, "an employee." 15 U.S.C. § 78d-1(a). Petitioners do not explain why this broad delegation authority does not encompass delegation of the power to hire ALJs.

To the extent petitioners contend that the word "agency" in § 3105 precludes delegation because it necessarily refers only to the head of the agency, that construction is implausible. For example, the very next section of the Code uses the phrase "the head of an Executive department." 5 U.S.C. § 3106. And Title 5 elsewhere uses the term "agency head." *E.g.*, *id.* § 608. Had Congress intended that ALJs could be appointed only by a department head, it

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ment head). Congress, of course, ultimately decided that hearing examiners would be "appointed and removed within the usual framework of the public service," *id.* at 50, an arrangement that raised no constitutional concerns at all.

Petitioners also incorrectly contend that the Attorney General, when asked to opine on the extent of the Civil Service Commission's authority under section 11 of the APA, deemed hearing examiners constitutional officers. Pet. Br. 37; *see Administrative Procedure Act, Promotion of Hearing Examiners*, 41 Op. Att'y Gen. 74 (1951). The Attorney General instead concluded that section 11 would pose no Appointments Clause problem *even if* ALJs were inferior officers. *See id.* at 79-80. The Attorney General therefore did not have to—and in fact did not—consider whether ALJs actually were inferior officers.

would have used one of those readily available formulations. The fact that Congress did not do so confirms that it considered ALJs employees that need not be appointed under the Appointments Clause.

III. THE COURT HAS NOT INSTRUCTED THE COURT-APPOINTED *AMICUS* TO BRIEF THE PARTIES' REMEDIAL AND REMOVAL ARGUMENTS

Petitioners present arguments about the appropriate remedy for an Appointments Clause violation. Pet. Br. 42-58. The Solicitor General, meanwhile, argues that if the Court reverses the court of appeals as to the Appointments Clause question, it should also consider whether Congress's decision to grant ALJs "good cause" removal protection is unconstitutional, and whether the Court can avoid that question by construing "for cause" and the Merit System Protection Board's authority under 5 U.S.C. § 7521 narrowly. Resp. Br. 39-55. This brief does not consider those questions because the Court has not instructed Court-appointed *amicus* to take a position on them.

A. *Amicus* was appointed to "brief and argue this case ... in support of the judgment below." 138 S. Ct. 923. Petitioners' remedial arguments by their terms are relevant only if the judgment below is reversed. The Court has thus not instructed the Court-appointed *amicus* to address those arguments.

B. So too with the Solicitor General's removal argument. The judgment below rests on the conclusion that SEC ALJs are not constitutional officers. The Solicitor General argues that the Court should

reach the removal question "[s]hould the Court agree that the Commission's ALJs are officers." Resp. Br. 39-40 n.7. If the Court concludes that SEC ALJs are officers under the Appointments Clause, the judgment below would be reversed regardless of the answer to the removal question. *See* Pet. Cert. Reply 11. Because any argument as to removal would not be in support of the judgment below, it is similarly outside the scope of *amicus*'s appointment.

Moreover, the Court has indicated that the removal issue is not properly before it. The Solicitor General asked the Court at the certiorari stage to add an additional question concerning removal if the Court did not believe that issue to be within the scope of the question presented in the petition. Resp. Cert. Br. 21, 26. Petitioners objected, explaining that the removal question was not "even remotely encompassed by petitioners' question presented," Pet. Cert. Reply 10, and presented several additional arguments for why the Court should not consider the removal question, including that it has never been decided by any court and that the answer would not affect the judgment, *id.* at 9-11. But petitioners specifically "requeste[d]" that if "the Court nevertheless [were] inclined to decide the removal issue now," that "the Court [should] formulate a specific question on that topic," as the Solicitor General had also requested. *Id.* at 11. This Court declined to add an additional question presented, indicating the Court's agreement with petitioners that the removal question is not properly before it.

CONCLUSION

For the foregoing reasons, the decision below should be affirmed.

Respectfully submitted,

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APPENDIX

RELEVANT CONSTITUTIONAL PROVISIONS

Article I, Section 6, Clause 2 of the United States Constitution (Incompatibility Clause):

* * *

[N]o Person holding any Office under the United States, shall be a Member of either House during his Continuance in Office.

Article I, Section 9, Clause 8 of the United States Constitution (Foreign Emoluments Clause):

No Title of Nobility shall be granted by the United States: And no Person holding any Office of Profit or Trust under them, shall, without the Consent of the Congress, accept of any present, Emolument, Office, or Title, of any kind whatever, from any King, Prince, or foreign State.

Article II, Section 2, Clause 2 of the United States Constitution (Appointments Clause):

* * *

[The President] shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

Article II, Section 4 of the United States Constitution (Impeachment Clause):

The President, Vice President and all civil Officers of the United States, shall be removed from Office on Impeachment for, and Conviction of, Treason, Bribery, or other high Crimes and Misdemeanors.

RELEVANT STATUTES

5 U.S.C. § 554:

Adjudications.

* * *

(d) The employee who presides at the reception of evidence pursuant to section 556 of this title shall make the recommended decision or initial decision required by section 557 of this title, unless he becomes unavailable to the agency. Except to the extent required for the disposition of ex parte matters as authorized by law, such an employee may not—

(1) consult a person or party on a fact in issue, unless on notice and opportunity for all parties to participate; or

(2) be responsible to or subject to the supervision or direction of an employee or agent engaged in the performance of investigative or prosecuting functions for an agency.

An employee or agent engaged in the performance of investigative or prosecuting functions for an agency in a case may not, in that or a factually related case, participate or advise in the decision, recommended decision, or agency review pursuant to section 557 of

this title, except as witness or counsel in public proceedings. This subsection does not apply—

(A) in determining applications for initial licenses;

(B) to proceedings involving the validity or application of rates, facilities, or practices of public utilities or carriers; or

(C) to the agency or a member or members of the body comprising the agency.

* * *

5 U.S.C. § 556:

Hearings; presiding employees; powers and duties; burden of proof; evidence; record as basis of decision.

(a) This section applies, according to the provisions thereof, to hearings required by section 553 or 554 of this title to be conducted in accordance with this section.

(b) There shall preside at the taking of evidence—

(1) the agency;

(2) one or more members of the body which comprises the agency; or

(3) one or more administrative law judges appointed under section 3105 of this title.

This subchapter does not supersede the conduct of specified classes of proceedings, in whole or in part, by or before boards or other employees specially provided for by or designated under statute. The func-

tions of presiding employees and of employees participating in decisions in accordance with section 557 of this title shall be conducted in an impartial manner. A presiding or participating employee may at any time disqualify himself. On the filing in good faith of a timely and sufficient affidavit of personal bias or other disqualification of a presiding or participating employee, the agency shall determine the matter as a part of the record and decision in the case.

(c) Subject to published rules of the agency and within its powers, employees presiding at hearings may—

(1) administer oaths and affirmations;

(2) issue subpenas authorized by law;

(3) rule on offers of proof and receive relevant evidence;

(4) take depositions or have depositions taken when the ends of justice would be served;

(5) regulate the course of the hearing;

(6) hold conferences for the settlement or simplification of the issues by consent of the parties or by the use of alternative means of dispute resolution as provided in subchapter IV of this chapter;

(7) inform the parties as to the availability of one or more alternative means of dispute resolution, and encourage use of such methods;

(8) require the attendance at any conference held pursuant to paragraph (6) of at least one representative of each party who has authority to negotiate concerning resolution of issues in controversy;

(9) dispose of procedural requests or similar matters;

(10) make or recommend decisions in accordance with section 557 of this title; and

(11) take other action authorized by agency rule consistent with this subchapter.

* * *

5 U.S.C. § 557:

Initial decisions; conclusiveness; review by agency; submissions by parties; contents of decisions; record.

(a) This section applies, according to the provisions thereof, when a hearing is required to be conducted in accordance with section 556 of this title.

(b) When the agency did not preside at the reception of the evidence, the presiding employee or, in cases not subject to section 554(d) of this title, an employee qualified to preside at hearings pursuant to section 556 of this title, shall initially decide the case unless the agency requires, either in specific cases or by general rule, the entire record to be certified to it for decision. When the presiding employee makes an initial decision, that decision then becomes the decision of the agency without further proceedings unless there is an appeal to, or review on motion of, the agency within time provided by rule. On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision except as it may limit the issues on notice or by rule. When the agency makes the decision without having presided at the reception of the evidence, the presiding employee or an employee qualified to preside at hearings pursuant to section 556 of this title shall

first recommend a decision, except that in rule making or determining applications for initial licenses—

(1) instead thereof the agency may issue a tentative decision or one of its responsible employees may recommend a decision; or

(2) this procedure may be omitted in a case in which the agency finds on the record that due and timely execution of its functions imperatively and unavoidably so requires.

(c) Before a recommended, initial, or tentative decision, or a decision on agency review of the decision of subordinate employees, the parties are entitled to a reasonable opportunity to submit for the consideration of the employees participating in the decisions—

(1) proposed findings and conclusions; or

(2) exceptions to the decisions or recommended decisions of subordinate employees or to tentative agency decisions; and

(3) supporting reasons for the exceptions or proposed findings or conclusions.

The record shall show the ruling on each finding, conclusion, or exception presented. All decisions, including initial, recommended, and tentative decisions, are a part of the record and shall include a statement of—

(A) findings and conclusions, and the reasons or basis therefor, on all the material issues of fact, law, or discretion presented on the record; and

(B) the appropriate rule, order, sanction, relief, or denial thereof.

* * *

5 U.S.C. § 2104:

Officer.

(a) For the purpose of this title, "officer", except as otherwise provided by this section or when specifically modified, means a justice or judge of the United States and an individual who is—

(1) required by law to be appointed in the civil service by one of the following acting in an official capacity—

(A) the President;

(B) a court of the United States;

(C) the head of an Executive agency; or

(D) the Secretary of a military department;

(2) engaged in the performance of a Federal function under authority of law or an Executive act; and

(3) subject to the supervision of an authority named by paragraph (1) of this section, or the Judicial Conference of the United States, while engaged in the performance of the duties of his office.

(b) Except as otherwise provided by law, an officer of the United States Postal Service or of the Postal Regulatory Commission is deemed not an officer for purposes of this title.

5 U.S.C. § 2105:

Employee.

(a) For the purpose of this title, "employee", except as otherwise provided by this section or when specifically modified, means an officer and an individual who is—

(1) appointed in the civil service by one of the following acting in an official capacity—

(A) the President;

(B) a Member or Members of Congress, or the Congress;

(C) a member of a uniformed service;

(D) an individual who is an employee under this section;

(E) the head of a Government controlled corporation; or

(F) an adjutant general designated by the Secretary concerned under section 709(c) of title 32;

(2) engaged in the performance of a Federal function under authority of law or an Executive act; and

(3) subject to the supervision of an individual named by paragraph (1) of this subsection while engaged in the performance of the duties of his position.

* * *

5 U.S.C. § 3105:

Appointment of administrative law judges.

Each agency shall appoint as many administrative law judges as are necessary for proceedings required to be conducted in accordance with sections 556 and 557 of this title. Administrative law judges shall be assigned to cases in rotation so far as practicable, and may not perform duties inconsistent with their duties and responsibilities as administrative law judges.

5 U.S.C. § 5372:

Administrative law judges.

(a) For the purposes of this section, the term "administrative law judge" means an administrative law judge appointed under section 3105.

(b)(1)(A) There shall be 3 levels of basic pay for administrative law judges (designated as AL–1, 2, and 3, respectively), and each such judge shall be paid at 1 of those levels, in accordance with the provisions of this section.

(B) Within level AL–3, there shall be 6 rates of basic pay, designated as AL–3, rates A through F, respectively. Level AL–2 and level AL–1 shall each have 1 rate of basic pay.

(C) The rate of basic pay for AL–3, rate A, may not be less than 65 percent of the rate of basic pay for level IV of the Executive Schedule, and the rate of basic pay for AL–1 may not exceed the rate for level IV of the Executive Schedule.

(2) The Office of Personnel Management shall determine, in accordance with procedures which the Office shall by regulation prescribe, the level in which each administrative-law-judge position shall be placed and the qualifications to be required for appointment to each level.

(3) (A) Upon appointment to a position in AL–3, an administrative law judge shall be paid at rate A of AL–3, and shall be advanced successively to rates B, C, and D of that level at the beginning of the next pay period following completion of 52 weeks of service in the next lower rate, and to rates E and F of that level

at the beginning of the next pay period following completion of 104 weeks of service in the next lower rate.

(B) The Office of Personnel Management may provide for appointment of an administrative law judge in AL–3 at an advanced rate under such circumstances as the Office may determine appropriate.

(4) Subject to paragraph (1), effective at the beginning of the first applicable pay period commencing on or after the first day of the month in which an adjustment takes effect under section 5303 in the rates of basic pay under the General Schedule, each rate of basic pay for administrative law judges shall be adjusted by an amount determined by the President to be appropriate.

(c) The Office of Personnel Management shall prescribe regulations necessary to administer this section.

5 U.S.C. § 7521:

Actions against administrative law judges.

(a) An action may be taken against an administrative law judge appointed under section 3105 of this title by the agency in which the administrative law judge is employed only for good cause established and determined by the Merit Systems Protection Board on the record after opportunity for hearing before the Board.

(b) The actions covered by this section are—

(1) a removal;

(2) a suspension;

(3) a reduction in grade;

(4) a reduction in pay; and

(5) a furlough of 30 days or less;

but do not include—

(A) a suspension or removal under section 7532 of this title;

(B) a reduction-in-force action under section 3502 of this title; or

(C) any action initiated under section 1215 of this title.

15 U.S.C. § 78d-1:

Delegation of functions by Commission.

(a) *Authorization; functions delegable; eligible persons; application of other laws.*

In addition to its existing authority, the Securities and Exchange Commission shall have the authority to delegate, by published order or rule, any of its functions to a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee board, including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter. Nothing in this section shall be deemed to supersede the provisions of section 556(b) of Title 5, or to authorize the delegation of the function of rulemaking as defined in subchapter II of chapter 5 of Title 5, with reference to general rules as distinguished from rules of particular applicability, or of the making of any rule pursuant to section 78s(c) of this title.

(b) *Right of review; procedure.*

With respect to the delegation of any of its functions, as provided in subsection (a) of this section, the Commission shall retain a discretionary right to review the action of any such division of the Commission, individual Commissioner, administrative law judge, employee, or employee board, upon its own initiative or upon petition of a party to or intervenor in such action, within such time and in such manner as the Commission by rule shall prescribe. The vote of one member of the Commission shall be sufficient to bring any such action before the Commission for review. A person or party shall be entitled to review by the Commission if he or it is adversely affected by action at a delegated level which (1) denies any request for action pursuant to section 77h(a) or section 77h(c) of this title or the first sentence of section 78*l*(d) of this title; (2) suspends trading in a security pursuant to section 78*l*(k) of this title; or (3) is pursuant to any provision of this chapter in a case of adjudication, as defined in section 551 of Title 5, not required by this chapter to be determined on the record after notice and opportunity for hearing (except to the extent there is involved a matter described in section 554(a)(1) through (6) of such Title 5).

(c) *Finality of delegated action.*

If the right to exercise such review is declined, or if no such review is sought within the time stated in the rules promulgated by the Commission, then the action of any such division of the Commission, individual Commissioner, administrative law judge, employee, or employee board, shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission.

15 U.S.C. § 78u:

Investigations and actions.

* * *

(c) *Judicial enforcement of investigative power of Commission; refusal to obey subpena; criminal sanctions.*

In case of contumacy by, or refusal to obey a subpena issued to, any person, the Commission may invoke the aid of any court of the United States within the jurisdiction of which such investigation or proceeding is carried on, or where such person resides or carries on business, in requiring the attendance and testimony of witnesses and the production of books, papers, correspondence, memoranda, and other records. And such court may issue an order requiring such person to appear before the Commission or member or officer designated by the Commission, there to produce records, if so ordered, or to give testimony touching the matter under investigation or in question; and any failure to obey such order of the court may be punished by such court as a contempt thereof. All process in any such case may be served in the judicial district whereof such person is an inhabitant or wherever he may be found. Any person who shall, without just cause, fail or refuse to attend and testify or to answer any lawful inquiry or to produce books, papers, correspondence, memoranda, and other records, if in his power so to do, in obedience to the subpena of the Commission, shall be guilty of a misdemeanor and, upon conviction, shall be subject to a fine of not more than $1,000 or to imprisonment for a term of not more than one year, or both.

* * *

RELEVANT REGULATIONS

17 C.F.R. § 200.14:

Office of Administrative Law Judges.

(a) Under the Administrative Procedure Act (5 U.S.C. 551-559) and the federal securities laws, the Office of Administrative Law Judges conducts hearings in proceedings instituted by the Commission. The Administrative Law Judges are responsible for the fair and orderly conduct of the proceedings and have the authority to:

(1) Administer oaths and affirmations;

(2) Issue subpoenas;

(3) Rule on offers of proof;

(4) Examine witnesses;

(5) Regulate the course of a hearing;

(6) Hold pre-hearing conferences;

(7) Rule upon motions; and

(8) Unless waived by the parties, prepare an initial decision containing the conclusions as to the factual and legal issues presented, and issue an appropriate order.

(b) The Chief Administrative Law Judge performs the duties of an Administrative Law Judge under the Administrative Procedure Act and the duties delegated to him or her by the Commission that are compatible with those duties. The Chief Administrative Law Judge is responsible for the orderly functioning of the Office of Administrative Law Judges apart from the conduct of administrative proceedings and acts as liaison between that Office and the Commission.

17 C.F.R. § 201.110:

Presiding officer.

All proceedings shall be presided over by the Commission or, if the Commission so orders, by a hearing officer. When the Commission designates that the hearing officer shall be an administrative law judge, the Chief Administrative Law Judge shall select, pursuant to 17 CFR 200.30-10, the administrative law judge to preside.

17 C.F.R. § 201.111:

Hearing officer: Authority.

The hearing officer shall have the authority to do all things necessary and appropriate to discharge his or her duties. No provision of these Rules of Practice shall be construed to limit the powers of the hearing officer provided by the Administrative Procedure Act, 5 U.S.C. 556, 557. The powers of the hearing officer include, but are not limited to, the following:

(a) Administering oaths and affirmations;

(b) Issuing subpoenas authorized by law and revoking, quashing, or modifying any such subpoena;

(c) Receiving relevant evidence and ruling upon the admission of evidence and offers of proof;

(d) Regulating the course of a proceeding and the conduct of the parties and their counsel;

(e) Holding prehearing and other conferences as set forth in § 201.221 and requiring the attendance at any such conference of at least one representative of each

party who has authority to negotiate concerning the resolution of issues in controversy;

(f) Recusing himself or herself upon motion made by a party or upon his or her own motion;

(g) Ordering, in his or her discretion, in a proceeding involving more than one respondent, that the interested division indicate, on the record, at least one day prior to the presentation of any evidence, each respondent against whom that evidence will be offered;

(h) Subject to any limitations set forth elsewhere in these Rules of Practice, considering and ruling upon all procedural and other motions, including a motion to correct a manifest error of fact in the initial decision. A motion to correct is properly filed under this Rule only if the basis for the motion is a patent misstatement of fact in the initial decision. Any motion to correct must be filed within ten days of the initial decision. A brief in opposition may be filed within five days of a motion to correct. The hearing officer shall have 20 days from the date of filing of any brief in opposition filed to rule on a motion to correct;

(i) Preparing an initial decision as provided in § 201.360;

(j) Upon notice to all parties, reopening any hearing prior to the filing of an initial decision therein, or, if no initial decision is to be filed, prior to the time fixed for the filing of final briefs with the Commission; and

(k) Informing the parties as to the availability of one or more alternative means of dispute resolution, and encouraging the use of such methods.

17 C.F.R. § 201.155:

Default; motion to set aside default.

(a) A party to a proceeding may be deemed to be in default and the Commission or the hearing officer may determine the proceeding against that party upon consideration of the record, including the order instituting proceedings, the allegations of which may be deemed to be true, if that party fails:

(1) To appear, in person or through a representative, at a hearing or conference of which that party has been notified;

(2) To answer, to respond to a dispositive motion within the time provided, or otherwise to defend the proceeding; or

(3) To cure a deficient filing within the time specified by the commission or the hearing officer pursuant to § 201.180(b).

(b) A motion to set aside a default shall be made within a reasonable time, state the reasons for the failure to appear or defend, and specify the nature of the proposed defense in the proceeding. In order to prevent injustice and on such conditions as may be appropriate, the hearing officer, at any time prior to the filing of the initial decision, or the Commission, at any time, may for good cause shown set aside a default.

17 C.F.R. § 201.180:

Sanctions.

(a) *Contemptuous conduct—*

(1) *Subject to exclusion or suspension.* Contemptuous conduct by any person before the Commission or a hearing officer during any proceeding, including at or in connection with any conference, deposition or hearing, shall be grounds for the Commission or the hearing officer to:

(i) Exclude that person from such deposition, hearing or conference, or any portion thereof; and/or

(ii) Summarily suspend that person from representing others in the proceeding in which such conduct occurred for the duration, or any portion, of the proceeding.

(2) *Review procedure.* A person excluded from a deposition, hearing or conference, or a counsel summarily suspended from practice for the duration or any portion of a proceeding, may seek review of the exclusion or suspension by filing with the Commission, within three days of the exclusion or suspension order, a motion to vacate the order. The Commission shall consider such motion on an expedited basis as provided in § 201.500.

(3) *Adjournment.* Upon motion by a party represented by counsel subject to an order of exclusion or suspension, an adjournment shall be granted to allow the retention of new counsel. In determining the length of an adjournment, the Commission or hearing officer shall consider, in addition to the factors set forth in § 201.161, the availability of co-counsel for the party or of other members of a suspended counsel's firm.

(b) *Deficient filings; leave to cure deficiencies.* The Commission or the hearing officer may reject, in whole or in part, any filing that fails to comply with

any requirements of these Rules of Practice or of any order issued in the proceeding in which the filing was made. Any such filings shall not be part of the record. The Commission or the hearing officer may direct a party to cure any deficiencies and to resubmit the filing within a fixed time period.

(c) *Failure to make required filing or to cure deficient filing.* The Commission or the hearing officer may enter a default pursuant to § 201.155, dismiss one or more claims, decide the particular claim(s) at issue against that person, or prohibit the introduction of evidence or exclude testimony concerning that claim if a person fails:

(1) To make a filing required under these Rules of Practice; or

(2) To cure a deficient filing within the time specified by the Commission or the hearing officer pursuant to paragraph (b) of this section.

17 C.F.R. § 201.360:

Initial decision of hearing officer and timing of hearing.

(a)(1) *When required.* Unless the Commission directs otherwise, the hearing officer shall prepare an initial decision in any proceeding in which the Commission directs a hearing officer to preside at a hearing, provided, however, that an initial decision may be waived by the parties with the consent of the hearing officer pursuant to § 201.202.

(2) *Time period for filing initial decision and for hearing—*

(i) *Initial decision.* In the order instituting proceedings, the Commission will specify a time period in which the hearing officer's initial decision must be filed with the Secretary. In the Commission's discretion, after consideration of the nature, complexity, and urgency of the subject matter, and with due regard for the public interest and the protection of investors, this time period will be either 30, 75, or 120 days. The time period will run from the occurrence of the following events:

(A) The completion of post-hearing briefing in a proceeding where the hearing has been completed; or

(B) The completion of briefing on a § 201.250 motion in the event the hearing officer has determined that no hearing is necessary; or

(C) The determination by the hearing officer that, pursuant to § 201.155, a party is deemed to be in default and no hearing is necessary.

(ii) *Hearing.* Under the 120-day timeline, the hearing officer shall issue an order scheduling the hearing to begin approximately four months (but no more than ten months) from the date of service of the order instituting the proceeding. Under the 75-day timeline, the hearing officer shall issue an order scheduling the hearing to begin approximately 2½ months (but no more than six months) from the date of service of the order instituting the proceeding. Under the 30-day timeline, the hearing officer shall issue an order scheduling the hearing to begin approximately one month (but no more than four months) from the date of service of the order instituting the proceeding. These deadlines confer no substantive rights on respondents. If a stay is granted pursuant

to § 201.161(c)(2)(i) or § 201.210(c)(3), the time period specified in the order instituting proceedings in which the hearing officer's initial decision must be filed with the Secretary, as well as any other time limits established in orders issued by the hearing officer in the proceeding, shall be automatically tolled during the period while the stay is in effect.

(3) *Certification of extension; motion for extension.*

(i) In the event that the hearing officer presiding over the proceeding determines that it will not be possible to file the initial decision within the specified period of time, the hearing officer may certify to the Commission in writing the need to extend the initial decision deadline by up to 30 days for case management purposes. The certification must be issued no later than 30 days prior to the expiration of the time specified for the issuance of an initial decision and be served on the Commission and all parties in the proceeding. If the Commission has not issued an order to the contrary within 14 days after receiving the certification, the extension set forth in the hearing officer's certification shall take effect.

(ii) Either in addition to a certification of extension, or instead of a certification of extension, the Chief Administrative Law Judge may submit a motion to the Commission requesting an extension of the time period for filing the initial decision. First, the hearing officer presiding over the proceeding must consult with the Chief Administrative Law Judge. Following such consultation, the Chief Administrative Law Judge may determine, in his or her discretion, to submit a motion to the Commission requesting an extension of the time period for filing the initial decision. This motion may request an extension of any

length but must be filed no later than 15 days prior to the expiration of the time specified in the certification of extension, or if there is no certification of extension, 30 days prior to the expiration of the time specified in the order instituting proceedings. The motion will be served upon all parties in the proceeding, who may file with the Commission statements in support of or in opposition to the motion. If the Commission determines that additional time is necessary or appropriate in the public interest, the Commission shall issue an order extending the time period for filing the initial decision.

(iii) The provisions of this paragraph (a)(3) confer no rights on respondents.

(b) *Content.* An initial decision shall include findings and conclusions, and the reasons or basis therefor, as to all the material issues of fact, law or discretion presented on the record and the appropriate order, sanction, relief, or denial thereof. The initial decision shall also state the time period, not to exceed 21 days after service of the decision, except for good cause shown, within which a petition for review of the initial decision may be filed. The reasons for any extension of time shall be stated in the initial decision. The initial decision shall also include a statement that, as provided in paragraph (d) of this section:

(1) The Commission will enter an order of finality as to each party unless a party or an aggrieved person entitled to review timely files a petition for review of the initial decision or a motion to correct a manifest error of fact in the initial decision with the hearing officer, or the Commission determines on its own initiative to review the initial decision; and

(2) If a party or an aggrieved person entitled to review timely files a petition for review or a motion to correct a manifest error of fact in the initial decision with the hearing officer, or if the Commission takes action to review as to a party or an aggrieved person entitled to review, the initial decision shall not become final as to that party or person.

(c) *Filing, service and publication.* The Secretary shall promptly serve the initial decision upon the parties and shall promptly publish notice of the filing thereof on the SEC Web site. Thereafter, the Secretary shall publish the initial decision in the SEC Docket; provided, however, that in nonpublic proceedings no notice shall be published unless the Commission otherwise directs.

(d) *Finality.*

(1) If a party or an aggrieved person entitled to review timely files a petition for review or a motion to correct a manifest error of fact in the initial decision, or if the Commission on its own initiative orders review of a decision with respect to a party or a person aggrieved who would be entitled to review, the initial decision shall not become final as to that party or person.

(2) If a party or aggrieved person entitled to review fails to file timely a petition for review or a motion to correct a manifest error of fact in the initial decision, and if the Commission does not order review of a decision on its own initiative, the Commission will issue an order that the decision has become final as to that party. The decision becomes final upon issuance of the order. The order of finality shall state the date on which sanctions, if any, take effect. Notice of the

order shall be published in the SEC Docket and on the SEC Web site.

17 C.F.R. § 201.410:

Appeal of initial decisions by hearing officers.

(a) *Petition for review; when available.* In any proceeding in which an initial decision is made by a hearing officer, any party, and any other person who would have been entitled to judicial review of the decision entered therein if the Commission itself had made the decision, may file a petition for review of the decision with the Commission.

(b) *Procedure.* The petition for review of an initial decision shall be filed with the Commission within such time after service of the initial decision as prescribed by the hearing officer pursuant to § 201.360(b) unless a party has filed a motion to correct an initial decision with the hearing officer. If such correction has been sought, a party shall have 21 days from the date of the hearing officer's order resolving the motion to correct to file a petition for review. The petition shall set forth a statement of the issues presented for review under § 201.411(b). In the event a petition for review is filed, any other party to the proceeding may file a cross-petition for review within the original time allowed for seeking review or within ten days from the date that the petition for review was filed, whichever is later.

(c) *Length limitation.* Except with leave of the Commission, the petition for review shall not exceed three pages in length. Incorporation of pleadings or filings by reference into the petition is not permitted. Motions to file petitions in excess of those limitations are disfavored.

(d) *Financial disclosure statement requirement.* Any person who files a petition for review of an initial decision that asserts that person's inability to pay either disgorgement, interest or a penalty shall file with the opening brief a sworn financial disclosure statement containing the information specified in § 201.630(b).

(e) *Prerequisite to judicial review.* Pursuant to Section 704 of the Administrative Procedure Act, 5 U.S.C. 704, a petition to the Commission for review of an initial decision is a prerequisite to the seeking of judicial review of a final order entered pursuant to such decision.

17 C.F.R. § 201.411:

Commission consideration of initial decisions by hearing officers.

(a) *Scope of review.* The Commission may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part, an initial decision by a hearing officer and may make any findings or conclusions that in its judgment are proper and on the basis of the record.

(b) *Standards for granting review pursuant to a petition for review—*

(1) *Mandatory review.* After a petition for review has been filed, the Commission shall review any initial decision that:

(i) Denies any request for action pursuant to Section 8(a) or Section 8(c) of the Securities Act of 1933, 15 U.S.C. 77h(a), (c), or the first sentence of Section 12(d) of the Exchange Act, 15 U.S.C. 78*l*(d);

(ii) Suspends trading in a security pursuant to Section 12(k) of the Exchange Act, 15 U.S.C. 78*l*(k); or

(iii) Is in a case of adjudication (as defined in 5 U.S.C. 551) not required to be determined on the record after notice and opportunity for hearing (except to the extent there is involved a matter described in 5 U.S.C. 554(a) (1) through (6)).

(2) *Discretionary review.* The Commission may decline to review any other decision. In determining whether to grant review, the Commission shall consider whether the petition for review makes a reasonable showing that:

(i) A prejudicial error was committed in the conduct of the proceeding; or

(ii) The decision embodies:

(A) A finding or conclusion of material fact that is clearly erroneous; or

(B) A conclusion of law that is erroneous; or

(C) An exercise of discretion or decision of law or policy that is important and that the Commission should review.

(c) *Commission review other than pursuant to a petition for review.* The Commission may, on its own initiative, order review of any initial decision, or any portion of any initial decision, within 21 days after the end of the period established for filing a petition for review pursuant to § 201.410(b). A party who does not intend to file a petition for review, and who desires the Commission's determination whether to order review on its own initiative to be made in a shorter time,

may make a motion for an expedited decision, accompanied by a written statement that the party waives its right to file a petition for review. The vote of one member of the Commission, conveyed to the Secretary, shall be sufficient to bring a matter before the Commission for review.

(d) *Limitations on matters reviewed.* Review by the Commission of an initial decision shall be limited to the issues specified in an opening brief that complies with § 201.450(b), or the issues, if any, specified in the briefing schedule order issued pursuant to § 201.450(a). Any exception to an initial decision not supported in an opening brief that complies with § 201.450(b) may, at the discretion of the Commission, be deemed to have been waived by the petitioner. On notice to all parties, however, the Commission may, at any time prior to issuance of its decision, raise and determine any other matters that it deems material, with opportunity for oral or written argument thereon by the parties.

(e) *Summary affirmance.*

(1) At any time within 21 days after the filing of a petition for review pursuant to § 201.410(b), any party may file a motion in accordance with § 201.154 asking that the Commission summarily affirm an initial decision. Any party may file an opposition and reply to such motion in accordance with § 201.154. Pending determination of the motion for summary affirmance, the Commission, in its discretion, may delay issuance of a briefing schedule order pursuant to § 201.450.

(2) Upon consideration of the motion and any opposition or upon its own initiative, the Commission

may summarily affirm an initial decision. The Commission may grant summary affirmance if it finds that no issue raised in the initial decision warrants consideration by the Commission of further oral or written argument. The Commission will decline to grant summary affirmance upon a reasonable showing that a prejudicial error was committed in the conduct of the proceeding or that the decision embodies an exercise of discretion or decision of law or policy that is important and that the Commission should review.

(f) *Failure to obtain a majority.* In the event a majority of participating Commissioners do not agree to a disposition on the merits, the initial decision shall be of no effect, and an order will be issued in accordance with this result.

17 C.F.R. § 201.452:

Additional evidence.

Upon its own motion or the motion of a party, the Commission may allow the submission of additional evidence. A party may file a motion for leave to adduce additional evidence at any time prior to issuance of a decision by the Commission. Such motion shall show with particularity that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence previously. The Commission may accept or hear additional evidence, may remand the proceeding to a self-regulatory organization, or may remand or refer the proceeding to a hearing officer for the taking of additional evidence, as appropriate.

No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA AND RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR EQUITY DEALERS OF AMERICA AS *AMICUS CURIAE* SUPPORTING PETITIONERS

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INTEREST OF *AMICUS CURIAE*[1]

Equity Dealers of America (EDA) is a trade association that represents the retail and institutional equity capital markets interests of its financial services firm members. EDA members advise hardworking and retired Americans how to create and preserve wealth and provide Main Street businesses with access to capital and advisory services. The EDA believes fair, efficient, and competitively balanced equity capital markets are necessary to protect investors, advance financial independence, stimulate job creation, and increase prosperity. The EDA's mission is to promote public trust and confidence in the U.S. equity capital markets. The EDA advocates against one-size-fits-all, undifferentiated regulations that disproportionately impact middle-market financial services firms, small businesses, and retail investors.

The EDA works tirelessly with its members, regulators, and policymakers to promote financial inclusion, economic opportunity, and financial independence. In addition to policy advocacy and public outreach, the EDA hosts meetings on the equity markets to inform and educate its members on issues relevant to their businesses and to their clients. Professionals at EDA member firms actively engage in shaping and promoting the EDA's advocacy agenda by identifying regulatory and compliance concerns, and developing issue-specific white papers intended to

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[1] All parties have consented to the filing of this brief by blanket consent or letter. No counsel for a party has authored this brief in whole or in part, and no person other than *amicus curiae*, its members, and its counsel has made monetary contribution to the preparation or submission of this brief.

directly benefit EDA member firms, their clients, and investors.

Because the EDA advocates for the interests of middle-market financial services professionals, the EDA has a direct and substantial interest in this case. EDA's members at times find themselves part of administrative proceedings before the Securities and Exchange Commission's (SEC) administrative law judges (ALJs). Thus, the EDA has a particular interest in ensuring that the SEC's administrative proceedings are fair and afford its members due process.

SUMMARY OF ARGUMENT

This Court should reverse the judgment of the United States Court of Appeals for the District of Columbia. SEC ALJs "exercise significant authority pursuant to the laws of the United States." *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976). SEC ALJs therefore are inferior officers of the United States who must be appointed consistent with the Appointments Clause of the U.S. Constitution. U.S. Const. art. § II, 2, cl. 2. Because SEC ALJs oversee proceedings in which quasi-criminal penalties may be levied, they must be constitutionally appointed. Proper appointment of SEC ALJs is necessary to safeguard the liberty of SEC respondents in SEC proceedings. Yet, SEC ALJs are not appointed by the President, a court of law, or the head of a department. This Court should find that their appointments are unconstitutional, and reverse the decision of the D.C. Circuit. The appointment of SEC ALJs pursuant to the Appointments Clause is a critical first step in ensuring constitutionally adequate SEC proceedings.

The story of the SEC is the story of a regulatory agency that has slowly but steadily expanded its reach and its nearly unfettered ability to interpret and enforce the nation's securities laws. Throughout its existence, the SEC's powers have been expanded to allow the agency to enforce securities laws not only against regulated companies, but also against unregulated companies and individuals as well. As the SEC's mandate has grown, it has increasingly brought such enforcement actions in administrative proceedings before its in-house ALJs rather than in an Article III court.

When the SEC was created in the 1930s, "its enforcement powers were largely limited to seeking injunctions in federal district courts to enjoin violations of the securities laws, and the only express provision for administrative hearings was to suspend or expel member or officers of national securities exchanges." Jed S. Rakoff, PLI Securities Regulation Keynote Address: Is the SEC Becoming a Law Unto Itself? 3 (Nov. 5, 2014). As the SEC's powers expanded over the course of its existence, its ability to use administrative proceedings to enforce its mandate—including by seeking injunctions and civil monetary penalties—was limited to regulated entities. Pub. L. No. 101-429, 104 Stat. 931 (1990). If the SEC wanted to seek monetary penalties against unregulated entities, it had to proceed in federal court. See, *e.g.*, *Gupta* v. *SEC*, 796 F. Supp. 2d 503, 507 (S.D.N.Y. 2011).

In 2010, however, Congress passed the Dodd-Frank Act, which authorizes the SEC to seek monetary penalties through its administrative proceedings against *any* individual for a violation of

the securities laws. SEC ALJs now routinely handle matters that previously were the exclusive province of federal district court judges. See 15 U.S.C. 78d-1(a) (authorizing the SEC to delegate any of the Commission's functions to ALJs); 17 C.F.R. 200.14 (assigning ALJs responsibility "for the fair and orderly conduct of" SEC enforcement proceedings).

This expansion of SEC power has eroded the due process rights of SEC respondents who find themselves in the crosshairs of the SEC's Division of Enforcement (Division). SEC respondents—including *unregulated* entities and individuals—frequently are forced to defend themselves in administrative proceedings with fewer procedural safeguards than in Article III courts. When individual SEC respondents must face prosecution by an SEC attorney, in the SEC's forum, before an SEC ALJ, and without the constitutional procedural protections afforded in federal court, unsurprisingly, the SEC respondents rarely prevail.

The paucity of substantive and procedural safeguards of due process in SEC enforcement proceedings is particularly troublesome because ALJs are not even constitutionally appointed. Even this minimal due process check is left wanting. An agency with such far-reaching power and the ability to impose quasi-criminal penalties on "*any individual*" (registered and non-registered entities alike) must enforce laws and regulations through a constitutionally appointed actor. That is the purpose of the Appointments Clause. See *Buckley*, 424 U.S. at 126. The Appointments Clause "preserves * * * the Constitution's structural integrity" by ensuring that officials remain "accountable to political force and the

will of the people." See *Freytag* v. *Commissioner*, 501 U.S. 868, 878, 884 (1991). It is critical to the protection of SEC respondents' due process rights that ALJs be constitutionally appointed so that they can be held politically accountable for their conduct.

It was in this ill-constructed court that petitioners, like many other SEC respondents, found themselves in 2012, when the Division brought an action for violations of the Investment Advisors Act. The Division alleged that petitioners' client presentations on retirement wealth management strategy violated the Advisors Act. The ALJ found that the petitioners used misleading information when pitching their services to prospective clients, and imposed fines and a cease and desist order on petitioners. The ALJ further barred petitioner Raymond Lucia from associating with an investment advisor, broker, or dealer. See *In the Matter of Raymond J. Lucia Companies, Inc. & Raymond J. Lucia, Sr.*, Release No. 4190, 2015 WL 5172953 (Sept. 3, 2015).

The ALJ's decision violated the Constitution because the ALJ in this case, and all SEC ALJs, are without constitutional authority to issue decisions. As explained below, the SEC enforcement proceedings are constitutionally suspect under the best-case scenario—that is, with a constitutionally appointed ALJ. But that minimum protection is not even currently in place. Accordingly, to bring some measure of constitutional protection to SEC enforcement proceedings, the EDA respectfully requests that this court rule in favor of petitioners and hold that the SEC's ALJs are officers of the United States within the meaning of the Appointments Clause.

ARGUMENT

The constitutional appointment of SEC ALJs is critical to upholding the due process rights of individuals called before the SEC. SEC proceedings are "in some tension with Article III of the Constitution, the Due Process Clause of the Fifth Amendment, and the Seventh Amendment right to a jury trial in civil cases." *Lorenzo* v. *SEC*, 872 F.3d 578, 602 (D.C. Cir. 2017) (citing P. Hamburger, Is Administrative Law Unlawful? 227-57 (2014)). Multiple aspects of the SEC's administrative proceedings curb the due process rights of SEC respondents by tilting the outcome in the SEC's favor. SEC enforcement actions are not like civil actions between private parties—they are "quasi criminal proceedings" with the power to impose sanctions that "look[] like criminal penalties." See Tr. of Oral Argument at 34, *Gabelli* v. *SEC*, 568 U.S. 442 (2013) (No. 11-1274) (Breyer, J.); *Gabelli* v. *SEC*, 568 U.S. 442, 451 (2013) ("In a civil penalty action, the Government is not only a different kind of plaintiff, it seeks a different kind of relief."). Although an SEC proceeding may not explicitly be criminal in nature, it carries the same consequences as a criminal conviction—a sanction that imposes a lifetime bar from "the securities industry [is the] equivalent of capital punishment" to an individual's likelihood. *Saad* v. *SEC*, 718 F.3d 904, 905 (D.C. Cir. 2013).

Given the ramifications of such proceedings, an ALJ's status as a non-appointed adjudicator is troubling. Arguably, the very use of ALJs and Article I proceedings are unconstitutional. In the modern administrative state, federal agencies regularly exercise broad Article II legislative powers that have

been unconstitutionally delegated by Congress, and exercise Article III judicial power, usurping the constitutional prerogative of the federal courts. These violations of the doctrine of separation of powers threaten the liberty of every American. See *Morrison* v. *Olsen*, 487 U.S. 654, 693 (1988) ("[T]he system of separated powers and checks and balances established in the Constitution was regarded by the Framers as 'a self-executing safeguard against the encroachment or aggrandizement of one branch at the expense of the other.'" (citing *Buckley*, 424 U.S. at 122)). But separation of powers concerns are not the only ones. The premise that Article III review can somehow cleanse the unconstitutionality of Article I adjudication only doubles down on violations of separation of powers. "An agency's interpretation of a statute that it administers receives considerable deference under current law." See Gary Lawson, *The Rise and Rise of the Administrative State*, 107 Harv. L. Rev. 1231, 1247 (1994). "More fundamentally, agency *fact-finding* is generally subject to deferential review under numerous statutes that expressly require courts to affirm agency factual conclusions that are supported by 'substantial evidence.' This kind of deferential review arguably fails to satisfy Article III." *Ibid.*

Those constitutional concerns of Article I rulings are compounded by SEC enforcement that contains shortcomings in substantive and procedural safeguards. For example, the SEC's Rules of Practice limit the time in which enforcement cases must be tried to an initial decision, they restrict the ability of SEC respondents to conduct discovery, and they allow the admission of damaging hearsay evidence that would not be permitted in an Article III court. The

discovery limitations imposed on SEC respondents is especially worrisome, given that, upon review of a Commission determination in a federal court, the court is limited to the record created before the Commission. Where an SEC respondent has limited ability to create the record in the proceedings below, Article III review is ineffective. As a result of those shortcomings, the Division's preferred forum—administrative proceedings before SEC ALJs—deprives SEC respondents of procedural rights they would be afforded in Article III courts and infringes upon their due process rights.

Considering the Article I proceedings' shaky constitutional footing, it is even more important that the presiding ALJs are appointed in accordance with the Constitution.

I. The Procedural and Evidentiary Limitations Before ALJs in Administrative Hearings Deprive SEC Respondents of their Due Process Rights.

Proceedings before an SEC ALJ lack the procedural protections available to defendants in federal court. Those limits deprive the SEC respondents of their due process rights. The SEC imposes an accelerated schedule mandated by the Rules of Practice, places extreme limitations on discovery, and yet, at the same time, gives the SEC power to introduce evidence that would not be admissible in an Article III court.

Where companies and individuals must face quasi-criminal proceedings that carry potentially ruinous fines and a loss of a license that could mean

the loss of a livelihood, companies and individuals called before an SEC ALJ are entitled to the full procedural protections and due process rights afforded under the Constitution.

A. The Litigation Timeframe Required by the Rules of Practice Deprives SEC Respondents of their Due Process Rights

The SEC's accelerated adjudication process deprives SEC respondents of the time necessary to develop their defenses and gives the SEC Enforcement Division an unfair advantage. SEC administrative actions proceeding in compressed timeframe to an initial decision. 17 C.F.R. 201.360(a)(2). A hearing officer is required to file an initial decision with the Secretary of the Commission either 30, 75, or 120 days after (1) the completion of post-hearing briefing, (2) the completion of briefing on a dispositive motion pursuant to 17 C.F.R. 201.250 in the event the ALJ determines no hearing is necessary, or (3) the determination by the ALJ that a party is in default pursuant to 17 C.F.R. 201.155 and no hearing is necessary. 17 C.F.R. 201.360(a)(2)(i). The Commission has complete discretion to choose the 30-, 75-, or 120-day timeline "after consideration of the nature, complexity, and urgency of the subject matter, and with due regard for the public interest and the protection of investors." *Ibid.* The Commission thereby chooses whether the proceedings will be accelerated to be concluded within a single month or up to 10 months. *Ibid.*

This compressed timeframe jeopardizes SEC respondents' due process rights and places SEC respondents at an unfair disadvantage. The Division

has years to prepare its case, documents, and other papers, limited only by the five-year statute of limitation under 28 U.S.C. 2462. Indeed, the Division has, in the past, conducted a "dump" of a "massive file," which took respondents months to process. *Chau v. SEC*, 72 F. Supp. 3d 417, 426-427 (S.D.N.Y. 2014). The condensed schedule denies SEC respondents a meaningful opportunity to gather evidence from key witnesses or examine the extensive evidence that the Division has collected in often an extended investigation. The SEC respondents thus frequently lack time to develop an effective defense to an action.

In contrast, Article III courts have the power to set case management and trial deadlines that take into account the needs of both parties, the complexity of the case, and the protection of the due process rights of the defendant. Due process requires that a defendant be given adequate time to prepare before a proceeding in which his or her professional license may be revoked. See, *e.g.*, *Nell* v. *United States*, 450 F.2d 1090, 1093 (4th Cir. 1971) (holding that due process requires that an attorney's disbarment or suspension proceedings be preceded by an opportunity to prepare a defense). The right of an SEC respondent to adequately prepare his or her case is threatened by the arbitrary and unfair limitations imposed by the Rules of Practice. Due process is not served when the Division can conduct a lengthy and detailed investigation against an SEC respondent, but the respondent must then prepare his or her defense within (at most) ten months of the order instituting proceedings.

B. The Discovery Procedures and Practices in the Administrative Forum Deprive SEC Respondents of their Due Process Rights

The lack of meaningful discovery also deprives SEC respondents of constitutionally required procedural safeguards. "The right to present evidence is, of course, essential to the fair hearing required by the Due Process Clause." *Jenkins* v. *McKeithen*, 395 U.S. 411, 429 (1969). This Court has held in a criminal context that although "the Due Process Clause has little to say regarding the amount of discovery which the parties must be afforded * * * it does speak to the balance of forces between the accused and his accuser." *Wardius* v. *Oregon*, 412 U.S. 470, 474 (1973). To avoid running afoul of the Due Process Clause, "discovery must be a two-way street." *Id.* at 475. In examining state criminal discovery practices, for example, this Court has been "particularly suspicious of state trial rules which provide nonreciprocal benefits to the State when the lack of reciprocity interferes with the defendant's ability to secure a fair trial." *Id.* at 474 n.6. Indeed, this Court has stated that "the State's inherent information-gathering advantages suggest that if there is to be any imbalance in discovery rights, *it should work in the defendant's favor*." *Id.* at 475 n.9 (emphasis added). This parity is absent in SEC proceedings and is in contrast to such parity in Article III adjudications.

1. SEC Rules of Practice governing discovery favor SEC.

In a quasi-criminal proceeding like one before an ALJ, the restrictions that the Rules of Practice place on a discovery violate the due process rights of SEC respondents.

Although an SEC respondent in an administrative proceeding is entitled to the Division's investigatory file (see 17 C.F.R. 201.230(a)(1)), the respondent's ability to obtain discovery is otherwise significantly more restricted than the permissive discovery allowed under the Federal Rules of Civil Procedure. Nor does an SEC respondent benefit from discovery rights afforded in criminal proceedings under the Federal Rules of Criminal Procedure, the Jenks Act, 18 U.S.C. 3500, *Brady* v. *Maryland*, 373 U.S. 83 (1963), and *Giglio* v. *United States*, 405 U.S. 150 (1972).

Two-way discovery is not required in SEC proceedings. The Division has the power to subpoena documents and conduct examinations of potential SEC respondents and witnesses during an investigation, but SEC respondents have no corresponding ability to make demands of the Division. Similarly, the Division is able to subpoena sworn testimony over the course of the investigation. But, a respondent is permitted only a limited number of depositions, and only if an order instituting proceedings has been entered. It is precisely this type of "imbalance in discovery rights" that this Court has criticized as unfair. See *Wardius*, 412 U.S. at 475 n.9.

a. *Document Collection*

The Rules of Practice state that, if the Division recommends that the Commission institute an administrative proceeding, the SEC respondent is entitled to "any party documents obtained by the Division prior to the institution of proceedings, in connection with the investigation leading to the Division's recommendation to institute proceedings." 17 C.F.R. 201.230(a)(1). Although the SEC is accordingly required to provide an SEC respondent with all of its discovery, SEC respondent have no ability to take their own discovery to rebut whatever the SEC has provided. Therefore, SEC respondents are forced to, in essence, litigate against themselves using the evidence the Division has obtained in making out its case against the SEC respondent. The rejection of reciprocal discovery stands in significant contrast to the protections afforded by constitutionally adequate tribunals.

b. *Interrogatories and Requests for Admission*

The Division is similarly advantaged over SEC respondents by its ability to use interrogatories, requests for admission, and other written discovery to build its case, with no reciprocal rights for SEC respondents. There is no provision in the Rules of Practice that permits SEC respondents to request other documents, make requests for admissions, or propound interrogatories, as would be permitted in federal court. Compare 15 U.S.C. 77s(c), with Fed. R. Civ. P. 33 and 36. The inability to use these discovery tools deprives SEC respondents of the ability to gain valuable insight into the strengths and weaknesses of

the Division's case. SEC respondents lose the ability to narrow issues for trial and define the claims of the Division. Moreover, the inability of SEC respondents to use interrogatories prevents them from collecting evidence that might otherwise be available. *United States* v. *W. Virginia Pulp & Paper Co.*, 36 F.R.D. 250, 251 (S.D.N.Y. 1964) ("The obtaining of evidence, or even information which may lead to evidence, from an adverse party is one of the functions of interrogatories. A further function is to obtain admissions and narrow the issues to be tried."); *United States* v. *Purdome*, 30 F.R.D. 338, 340 (W.D. Mo. 1962) ("[I]nterrogatories serve two distinct purposes: First, to ascertain facts and to procure evidence, or secure information as to where pertinent evidence exists and can be obtained; second, to narrow the issues."'). Depriving SEC respondents of the ability to secure critical information in advance of trial and to reduce the number of issues that need to be addressed at trial make SEC respondents' nearly insurmountable odds even longer.

c. *Depositions*

Similarly, the Division may, through informal and formal investigations, take testimony, request documents, and examine a prospective SEC respondent (and respondent's employees) for years before administrative proceedings are instituted. The Division is permitted to take sworn subpoenaed testimony as part of its investigation and introduce such testimony as evidence. See *In Re Del Mar Fin. Servs., Inc.*, Release No. 8314 (Oct. 24, 2003) (holding that ALJ should have admitted investigative transcripts that "contained evidence that was relevant to the issues in the case"). Indeed, the Division has broad authority to subpoena witnesses and compel

production of documents as part of its formal investigatory process. See Section 19(c) of the Securities Act, Section 21(b) of the Securities Exchange Act, Section 209(b) of the Advisers Act, and Section 42(b) of the Investment Company Act.

Yet, SEC respondents' ability to take depositions is again conversely limited. In administrative proceedings operating under the 120-day timeframe pursuant to Rule 360(a)(2), SEC respondents may notice three depositions per side in single-respondent proceedings and may collectively notice five depositions per side in multiple-respondent proceedings. 17 C.F.R. 201.233(a)(1)-(2). A respondent or the Division may file a motion with the ALJ seeking leave to notice two additional depositions if the movant "demonstrates a compelling need" by, among other things, "[d]escribing * * * why the deposition of each witness and proposed additional witness is necessary for the moving side's arguments, claims, or defenses[.]" *Id.* at 201.233(a)(3).

SEC respondents or the Division may also notice additional depositions of witnesses if the ALJ or the Commission finds that the prospective witness will give material testimony, is unavailable, and that the taking of the deposition will serve the interests of justice. 17 C.F.R. 201.233(b). However, that provision has been interpreted narrowly by ALJs who frequently deny SEC respondents' requests for additional depositions. See, *e.g.*, *In re Delany*, Admin. Proceedings Rulings Release No. 1652, 109 SEC Docket 2282, 2014 WL 11115571 at *5 (July 25, 2014) (denying joint request pursuant to Rule 233(b) for subpoena despite witness having Parkinson's disease); *In re Daxor Corp.*, Admin. Proceedings

Rulings Release No. 666, 100 SEC Docket 1750, 2011 WL 7820430 at *3-4 (Feb. 24, 2011) (denying deposition for witness who was one of three doctors in specialty who worked at "short-staffed" hospital system despite "personal and professional hardship" and showing that testifying would be an "extreme burden" for the witness).

Critically, in 30-day and 75-day actions, SEC respondents are not permitted to notice depositions by right at all, and may notice depositions only of unavailable persons pursuant to Rule 233(b). See *id.* at 201.233(b). The reluctance of SEC ALJs to grant depositions under that provision potentially leaves SEC respondents in 30- and 75-day actions without the ability to notice depositions at all. Accordingly, although the Rules of Practice appear to award each side the same number of depositions, as a practical matter the Division has far greater ability to compel testimony, particularly in the 30- and 75-day contexts where the Division is permitted to take testimony as part of its investigation but SEC respondents are left without a corresponding right to notice depositions.

2. The Federal Rules of Civil Procedure level the playing field to ensure due process is preserved.

The strict limitations of the Rules of Practice stand in stark contrast to the liberal discovery standards set forth in the Federal Rules of Civil Procedure. See, *e.g.*, *Swierkiewicz* v. *Sorema N.A.*, 534 U.S. 512 (2002) ("This simplified notice pleading standard relies on liberal discovery rules and summary judgment motions to define disputed facts

and issues and to dispose of unmeritorious claims."); *Katz* v. *Batavia Marine & Sporting Supplies, Inc.*, 984 F.2d 422, 424 (Fed. Cir. 1993) ("It is a premise of modern litigation that the Federal Rules contemplate liberal discovery, in the interest of just and complete resolution of disputes.").

Were the Division to bring its actions in federal court, it would no longer have an overwhelming advantage with respect to fact gathering and discovery. It would be required to respond to requests for admission and interrogatories, and would have to respond to requests for relevant documents beyond the Division's investigatory file. SEC respondents in 30-day and 75-day proceedings would have the right to take depositions, a right that is now effectively denied to them. And, SEC respondents in 120-day proceedings would be guaranteed the full complement of ten depositions per party, at least double what SEC respondents would receive under the Rules of Practice. Full and fair liberal discovery is a "premise of modern litigation" and necessary for a fair resolution of disputes. The Commission's extreme limits on discovery rights deprives SEC respondents of the ability of fully and fairly defend themselves in quasi-criminal proceedings before an ALJ and violates their due process rights.

C. The Evidentiary Rules in the Administrative Forum Deprive SEC Respondents of their Due Process Rights

In addition to the lack of parity in information-gathering powers between the Division and SEC respondents, the Rules of Practice give the Division wide latitude to use evidence against SEC respondents that would not be admissible in an Article III court. The permissive admissibility standard in the administrative forum favors the Division and allows convictions of SEC respondents for securities law violations based upon inadmissible evidence. A practice whereby hearsay or other ordinarily inadmissible evidence can be used to impose quasi-criminal penalties on SEC respondents is inconsistent with the principles of due process.

The Federal Rules of Evidence do not apply in administrative hearings before an SEC ALJ. An ALJ may receive any relevant evidence, and need only exclude evidence that is "irrelevant, immaterial, unduly repetitious, or unreliable." 17 C.F.R. 201.320(a). ALJs may admit all evidence that "can conceivably throw any light upon the controversy." *In re Jesse Rosenblum*, 47 SEC 1065, 1072 (1984). Even hearsay is admissible. *In re Leslie A. Arouh*, 99 SEC Docket 32306, 32323 (Sept. 13, 2010), see also *In re Del Mar Fin. Servs., Inc.*, Release No. 8314 (Oct. 24, 2003) ("We have stated on numerous occasions that the Federal Rules of Evidence, including the rules on hearsay, are not applicable to our administrative proceedings which favor liberality in the admission of evidence.").

As discussed above, the Division often seeks sanctions, including excessive monetary penalties or an industry bar, which are tantamount to criminal penalties. It is only fair that an SEC respondent is afforded the full panoply of procedural protections in a proceeding in which a government actor is seeking to deprive the respondent of his or her livelihood. The Federal Rules of Evidence serve an important gatekeeping function that protects defendants in federal court. *Daubert* v. *Merrell Dow Pharma.*, 509 U.S. 579, 587 (1993) ("That, nevertheless is the balance that is struck by the Rules of Evidence designed not for the exhaustive search for cosmic understanding but for the particularized resolution of legal disputes."). The rules have been carefully crafted by Congress to balance the interests of full disclosure of the relevant facts with the need to ensure reliability. By admitting hearsay evidence and otherwise disregarding federal evidentiary rules, the Rules of Practice disturb this carefully crafted balance and expose SEC respondents to quasi-criminal penalties without the full protection they deserve.

D. The Structure of the Administrative Hearing Deprives SEC Respondents of their Due Process Rights

SEC ALJs lack independence. They are part of the same administrative agency that is conducting the prosecution, making the regulations, and interpreting the applicable law. SEC respondents thus are forced to submit to an administrative hearing before an executive officer who decides their guilt or innocence, and imposes sanctions that can cripple livelihoods. This forum, in which the executive and adjudicative functions are performed by the same agency, does not

allow for a fair and impartial trial before an independent arbiter. See *Lawson*, 107 Harv. L. Rev. at 1248 ("The destruction of th[e] principle of separation of powers is perhaps the crowning jewel of the modern administrative revolution. Administrative agencies routinely combine all three governmental functions in the same body, and even the same people within that body."). SEC ALJs rarely exercise independence from the SEC in a way that safeguards the due process rights of SEC respondents. The partiality of the ALJs and their ability to control the administrative proceedings leaves many SEC respondents with little choice but to accept a settlement and admission of liability. The procedural hurdles discussed above combine with the SEC's built-in home court advantage to create an administrative forum in which a respondent is almost certain to be found liable. Indeed, over a five-year period from 2010 to 2015, the SEC won 95 percent of its administrative proceedings.[2]

The structural disadvantages continue throughout the proceedings. At no point over the course of an administrative hearing does an SEC respondent have an ability to develop a full and fair record before an Article III fact finder. From the outset of an investigation through the administrative proceedings, a respondent's ability to shape the record and collect evidence is limited. Even if the SEC respondent appeals to a federal court of appeals the procedural disadvantages continue to haunt them, as they are reliant on the limited discovery permitted and

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[2] See Jean Eaglesham, *SEC Wins With In-House Judges*, WALL ST. J. (May 6, 2015), http://www.wsj.com/articles/sec-wins-with-in-house-judges-1430965803.

evidence adduced in the administrative context to form the record for appeal.

II. The Lack of Meaningful Judicial Review of an ALJ Decision Deprives SEC Respondents of Their Due Process Rights

Should SEC respondents proceed through a hearing, procedural biases are rarely cured by a Commission that too frequently rubber stamps the outcomes of the hearings below. The Commission's determination is then subject to only limited federal review that is constrained by the record developed before the ALJ.

Although SEC respondents have a right to appeal the determination of an ALJ to the full Commission, *de novo* review by the Commission is anything but independent. See 17 C.F.R. 201.410. From 2010 to 2015, the Division won 88 percent of its appeals of ALJ decisions.[3] Such an overwhelming success rate is to be expected given the built-in procedural and evidentiary advantages the Division enjoys before the ALJ. The ALJ's ability to shape the record and the Commission's rubber stamping of the ALJs' determinations, creates a forum in which fair adjudication is rare, if not impossible.

A respondent's path gets no easier if he or she elects to take the case to a federal court of appeals. The ALJ is afforded significant deference on both factual and legal determinations. A court of appeals will review questions of fact decided by the ALJ under a "substantial evidence" standard. See *Universal*

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[3] *Ibid.*

Camera Corp. v. *NLRB*, 340 U.S. 474, 477 (1951). Legal determinations are accorded *Chevron* deference, which requires the court to defer to the SEC's reasonable interpretation of its own organic statute. See *Chevron, U.S.A., Inc.* v. *Nat. Res. Def. Council*, 467 U.S. 837, 844 (1984). A respondent's burden is even greater given the procedural inequities present at the administrative hearing. Because the federal appellate court is not empowered to take testimony, a respondent is limited to the record created before the SEC. Accordingly, judicial review by a court of appeals does not provide a sufficient remedy for the inequities inherent in the Commission's Rules of Practice.

III. SEC Enforcement Proceedings' Constitutional Infirmities Are Compounded Because ALJs Are Not Appointed Pursuant to the Appointments Clause

As explained above, SEC enforcement proceedings lack many of the hallmarks of due process protections provided in federal district court litigation.

These constitutional failings are exacerbated because the ALJs themselves are merely agency employees, not subject to the Appointments Clause. Such appointment would provide the imprimatur of the executive branch on SEC administrative proceedings before ALJs, because the ALJs would be answerable to the President. It is critical to the protection of SEC respondents' due process rights that ALJs be constitutionally appointed so that they are ultimately answerable to the will of the American people. The Appointments Clause is critical to

preserving that political accountability and thereby "the Constitution's structural integrity." See *Freytag*, 501 U.S. at 878, 884. ALJs wield great power in SEC proceedings—proceedings that are already rife with disparities between the SEC and SEC respondents. ALJs make critical evidentiary decisions over how the record is created and also provide legal interpretations of the statutory schemes. ALJs also, at the end of proceedings, levy individual sanctions that can prohibit individuals from working in any regulated financial service industry. Given the lack of constitutionally adequate safeguards that already permeate SEC proceedings, it is a bare minimum of due process protections for the person presiding over such proceedings to be appointed by the President and, ultimately, answerable to the President. That step is critical to ensuring constitutionally adequate due process protections.

* * *

The SEC has broad power to impose devastating penalties on companies and individuals. As this Court has remarked, the government "is not only a different kind of plaintiff, it seeks a different kind of relief." *Gabelli*, 568 U.S. at 451. The SEC has the ability to bar individuals from the securities industry and impose crippling punitive fines. These quasi-criminal penalties underscore the need to ensure that the due process rights of every respondent that practices before the SEC are protected. The Appointments Clause provides one such guarantee.

CONCLUSION

The judgment of the United States Court of Appeals for the District of Columbia Circuit should be reversed.

Respectfully submitted.

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No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA COMPANIES, INC. AND RAYMOND J. LUCIA,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF AMICUS CURIAE OF FEDERAL ADMINISTRATIVE LAW JUDGES CONFERENCE IN SUPPORT OF NEITHER PARTY

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STATEMENT OF INTEREST[1]

This brief is presented on behalf of the Federal Administrative Law Judges Conference (FALJC). FALJC is a voluntary professional association founded in 1947 that represents and serves administrative law judges (ALJs) employed throughout the federal government. The government employs more than 1930 ALJs in more than 30 agencies to adjudicate a wide variety of cases. Appendix A.[2]

FALJC membership includes ALJs from virtually every Federal agency that appoints ALJs. Appendix B (FALJC Mission and Leadership). A primary FALJC mission is to promote due process and impartiality in administrative procedure through maintenance of ALJ decisional independence under the Administrative Procedure Act, (APA) Pub. L. No. 79-404, 60 Stat. 237 (1946), codified at 5 U.S.C. §§ 551-559. Appendix B.

This Court granted certiorari on the question of whether ALJs of the Securities and Exchange Commission (SEC) are officers of the United States within

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[1] The parties have consented to the filing of this amicus brief. No person other than the Federal Administrative Law Judges Conference and its counsel have authored this brief in whole or in part or made any monetary contribution intended to fund the preparation or submission of the brief.

[2] ALJs adjudicate cases involving, among other things, advertising, antitrust, banking, communications, energy, environmental protection, food and drugs, health and safety, housing, interstate commerce including the United States Mail, international trade, labor management relations, securities and commodities markets, transportation, social security disability, Medicare, and other benefits claims.

the meaning of the Appointments Clause.[3] This issue has been raised regarding ALJs at other agencies and this decision will impact other agencies.[4] FALJC takes no position on the question of whether ALJs are officers.[5]

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[3] *Lucia v. SEC*, 868 F.3d 1021 (D.C. Cir. 2017), *cert. granted*, 2018 WL 386565 (U.S. Jan. 12, 2018) (No. 17-130). The Appointments Clause provides:

> [The President] shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the Supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

U.S. Const. art. II, § 2, cl. 2.

[4] Some ALJ members have been appointed by heads of agencies, some have had previous appointments ratified by the agency head, and some are appointed by an official that is not the head of a department or commission. All ALJs, however, were deemed qualified after an extensive examination process conducted by the Office of Personnel Management (OPM).

[5] Petitioner contends that administrative proceedings conducted by SEC administrative law judges are invalid because they are inferior officers under the Constitution and were not properly appointed as required by the Appointments Clause of the U.S. Constitution. Respondent agrees. The ruling en banc below split 5-5, rejected Petitioner's argument and followed D.C. Circuit precedent based on final decision-making authority. *See Landry v. FDIC*, 204 F.3d 1125 (D.C. Cir. 2000). In contrast, the Tenth Circuit in *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016) held that the SEC ALJs are inferior officers based on this Court's analysis that was applied to Special Trial Judges of the Tax Court in *Freytag v. Commissioner of Internal Revenue*, 501 U.S. 868 (1991). The majority ruling in *Bandimere* goes no further than

Resolution of the question presented is important to FALJC, however, for three principal reasons: to preserve ALJ decisional independence created by Congress in the APA; to clarify the remedy for an unconstitutional appointment process on final, pending, and prospective administrative adjudications throughout the federal government; and, to ensure that ratification of incumbent ALJs is sufficient under the Appointments Clause to permit ALJs to adjudicate existing and future disputes consistent with the Constitution.

SUMMARY OF ARGUMENT

Congress enacted the APA and created the ALJ position to provide for due process in administrative adjudication. The APA ensures due process through ALJ selection, appointment, protections, and independence.

The resolution of this proceeding should preserve ALJ decisional independence created by Congress in the APA, provide clear guidelines regarding the ratification or appointment of ALJs and the review of pending cases by properly-appointed ALJs, and insure that ratification of incumbent ALJs is sufficient under the Appointments Clause to permit ALJs to adjudicate existing and future disputes consistent with the Constitution.

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finding that SEC ALJs are inferior officers who were not appointed pursuant to Article II of the Constitution. It is noteworthy that the concurring opinion by Judge Briscoe and the dissent by Judge McKay address the potential impact of the majority ruling on administrative proceedings conducted by ALJs.

ARGUMENT

I. CONGRESS ENACTED THE APA AND CREATED THE ALJ POSITION TO PROVIDE FOR OPEN AND FAIR DUE PROCESS IN ADMINISTRATIVE ADJUDICATION FOR THE BENEFIT OF THE PUBLIC

Congress expressly enacted the APA "to improve the administration of justice by prescribing fair administrative procedure." Pub. L. No. 79-404, 60 Stat. 237 (1946). "The ALJ position was created by the Administrative Procedure Act (APA) to ensure fairness in administrative proceedings before Federal government agencies. ALJs have two primary duties which are 1) presiding over agency hearings, taking evidence, and acting as a preliminary fact finder in proceedings, and 2) making an initial determination about the resolution of a dispute." *See* Statement of Joseph Kennedy, Associate Director of Human Resources Solutions, U.S. Office of Personnel Management, *Examining Due Process in Administrative Hearings*, Hearing before the Subcomm. on Regulatory Affairs and Federal Management, U.S. Senate Comm. on Homeland Security and Governmental Affairs, 114th Cong., 2d Sess. (May 12, 2016).

To achieve this goal, the APA contains several essential prescriptions. The APA requires agencies to keep the public currently informed of agency organization, procedures, and rules. It provides for public participation in the rulemaking process. It prescribes uniform standards for the conduct of formal rulemaking and adjudicatory proceedings which are required by statute to be made on the record. It restates the law governing judicial review. Finally, the APA provides protection for the independence and status of

examiners to be used by agencies in the conduct of hearings. Ralph F. Fuchs, *The Attorney General's Manual on the Administrative Procedure Act*; *The Federal Administrative Procedure Act and the Administrative Agencies*, 23 Ind. L.J. 364 (1948). A hearing examiner is now called an Administrative Law Judge. *See* Sections 5 and 11 of the APA; U.S. Dep't of Justice, *Attorney General's Manual on the Administrative Procedure Act* 54-56, 72 (1947).

Prior to the APA, federal administrative agencies designated trial examiners to preside over hearings for the reception of evidence, but the examiners' tenure, status, compensation, and promotions were dependent on agency ratings under the Classification Act of 1923, as amended. *See Ramspeck v. Fed. Trial Exam'rs Conference*, 345 U.S. 128, 130 (1953). This regulatory system engendered many complaints that the trial examiners "were mere tools of the agency concerned and subservient to the agency heads in making their proposed findings of fact and recommendations." *Id.* Therefore, after extensive executive branch committee studies and reports and congressional hearings, Congress included Section 11 in the APA for the purpose of rendering trial examiners independent and secure in their tenure and compensation. *Id.* at 130 and n.2 (citing Administrative Procedure Act—Legislative History, S.Doc. No. 248, 79th Cong., 2d Sess., p. 215 (1946)). Section 11 of the APA provided that "[e]xaminers shall be removable by the agency in which they are employed only for good cause" and their "compensation is provided independent of the agency recommendations or ratings." *Id.*

This brief history demonstrates that Congress created the ALJ position under section 5 U.S.C. § 553(b)(3) of the APA to enhance procedural fairness and due process in administrative proceedings before federal agencies by allowing an impartial decision maker to preside over the reception of evidence at agency hearings. The task of a court in determining validity of a congressional enactment is not to destroy the act, but to construe it, if consistent with the will of Congress, so as to comport with constitutional limitations. *I.N.S. v. St. Cyr*, 533 U.S. 289 (2001); *Pub. Citizen v. Dep't of Just.*, 491 U.S. 440, 466 (1989).

Congress provided that "[e]ach agency shall appoint as many administrative law judges as are necessary for hearings required under the APA." 5 U.S.C. § 3105. Specifically, the APA provides that in rule-makings or adjudications required by statute to be determined on the record after opportunity for agency hearing, the agency, one or more members of the body which comprises the agency, or one or more Administrative Law Judges appointed under 5 U. S.C. § 3105 shall preside at the taking of evidence.[6]

ALJs serve as independent impartial triers of fact "insulated from political interference" when presiding over formal proceedings requiring a decision on the record after the opportunity for a hearing. *See Butz v. Economou*, 438 U.S. 478, 513 (1978). ALJs "exercise significant authority pursuant to the laws of the United States", *Buckley v. Valeo*, 424 U.S. 1, 126 (1976) (per curiam), to issue subpoenas, regulate dis-

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[6] Under 5 U.S.C. § 556, the agency head or one or more members of the agency may preside over agency adjudications. These alternatives are rarely used.

covery, conduct pre-hearing conferences, rule on procedural and dispositive motions, administer oaths, receive offers of proof and relevant evidence, regulate the course of the hearing, review briefs, and issue decisions and orders based on findings of fact and conclusions of law. *See generally* 5 U.S.C. §§ 556, 557 (2006); *see also Federal Maritime Commission v. S.C. State Ports Authority*, 535 U.S. 743, 757-759 (2002) (describing the similarities between FMC proceedings and civil litigation).

Whether this Court determines that SEC ALJs are inferior officers or employees, the plain wording of the APA and its legislative history shows the intent of Congress to provide for administrative adjudication procedures that are open to the public and conducted "on the record" by fair and impartial Administrative Law Judges.

II. CURRENT ALJ SELECTION, APPOINTMENT, PROTECTIONS, AND INDEPENDENCE UNDER THE APA

The Civil Service Reform Act of 1978 (CSRA), Pub.L. No. 95–454, 92 Stat. 1111 (1978), abolished the Civil Service Commission and distributed its functions primarily among three new agencies: the Office of Personnel Management (OPM), the Merit Systems Protection Board (MSPB), and the Federal Labor Relations Authority (FLRA). By statute, OPM has the duty to administer the ALJ examination and establish a list of eligible candidates from which agencies make competitive service selections of ALJs.

ALJ candidates must demonstrate an active law license in good standing, at least seven years of litigation or other qualifying experience, and achieve a

sufficient score on a multi-part competitive examination. U.S. Office of Personnel Management, Qualification Standard for Administrative Law Judge Position, *available at* https://www.opm.gov/policy-data-oversight/classification-qualifications/general-schedule-qualification-standards/specialty-areas/administrative-law-judge-positions/.

The ALJ examination measures thirteen judicial competencies necessary for successful ALJ performance.[7] The examination currently includes a timed situational judgment test, a timed writing sample, an untimed experience assessment, a four-hour written examination, a structured interview, and a logic-based measurement test. Appendix C; *see also* Erin Masson Wirth, *Becoming a United States Administrative Law Judge,* Careers in Administrative Law and Regulatory Practice, ABA Section of Administrative Law and Regulatory Practice (2017), *available at* https://www.americanbar.org/content/dam/aba/administrative/administrative_law/2017_Careers_Book_Wirth_Chapter_updated.authcheckdam.pdf.

Based on experience, examination scores, and veteran preference points, ALJ candidates who meet the minimum qualification standards and pass the examination are assigned a score and are ranked on a register of eligible candidates. Agencies needing to appoint ALJs select from an OPM certification that contains at least the three highest ranking candidates

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[7] A competency is a measurable pattern of knowledge, skills, abilities, behaviors, and other characteristics that a candidate needs to perform work roles or occupational functions successfully. OPM's ALJ competencies currently include decision making, interpersonal skills, judicial analysis, judicial decisiveness, judicial management, judicial temperament, litigation and courtroom competence, oral communication, problem solving, professionalism, reasoning, self-management, and writing.

for that geographical location. Agencies may also hire lateral transfers of current incumbent ALJs at other federal agencies. A number of agencies borrow ALJs from other agencies through the OPM loan program rather than hiring their own ALJs. 5 C.F.R. § 930.208.

Once appointed, ALJs have statutory protections and independence from political pressure or influence by the agency. To protect administrative law judges from improper agency influence, Congress provided in the APA that disciplinary or removal actions "may be taken against an administrative law judge appointed under [5 U.S.C. § 3105] by the agency in which the administrative law judge is employed only for good cause established and determined by the Merit Systems Protection Board on the record after opportunity for hearing before the Board." 5 U.S.C. § 7521(a) and (b).

When the APA requires a hearing to be conducted on the record and the agency head chooses not to preside at the reception of the evidence, the ALJ presides at the reception of evidence and issues an initial decision, unless the agency requires that the entire record be certified to it for decision. 5 U.S.C. § 557(a) and (b).

The APA provides that ALJs "shall make the recommended decision or initial decision required" and "may not (1) consult a person or party on a fact in issue, unless on notice and opportunity for all parties to participate, or (2) be responsible to or subject to the supervision or direction of an employee or agent engaged in the performance of investigative or prosecuting functions for an agency." 5 U.S.C. § 554(d)(1)-(2). "An employee or agent engaged in the performance of investigative or prosecuting functions for an agency in a case may not, in that or a factually related

case, participate or advise in the decision, recommended decision, or agency review . . . except as witness or counsel in public proceedings." 5 U.S.C. § 554(d)(2). However, the head of an agency retains authority over agency policy through the administrative appeals process.

While there are variations, ordinarily when an ALJ makes an initial decision, that decision may become the decision of the agency unless a party appeals the ALJ's initial decision or the agency decides to review the initial decision. "On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision except as it may limit the issues on notice or by rule." 5 U.S.C. § 557(b).

Agencies may modify or reverse ALJ decisions as to both fact and law, but when reviewing the initial decision, must give deference to credibility determinations, particularly those based on witness demeanor, and consider the ALJ's initial decision. *See* Kent Barnett, *Resolving the ALJ Quandary*, 66 Vand. L. Rev. 797, 806-07, n. 50 and 51 (2013) (citations omitted). Generally, an administrative adjudication only becomes a final agency action if approved on appeal by the agency head or agency designated appellate authority, or if there is no appeal from an initial decision.

III. THE REMEDIAL RAMIFICATIONS IF THE SEC ALJ APPOINTMENT PROCESS IS FOUND TO BE UNCONSTITUTIONAL

A. Final Judgments

This Court has held that even when an adjudicator lacks the power to decide a case, once a judgment becomes final, it cannot be attacked collaterally absent extraordinary circumstances that outweigh finality.

Travelers Indem. Co. v. Bailey, 557 U.S. 137, 154 (2009). *See also Durfee v. Duke*, 375 U.S. 106, 114-15 (1963); *James B. Beam Distilling Co. v. Georgia*, 501 U.S. 529, 540 (1991) (in civil cases there is little opportunity for collateral attack on final judgments). Otherwise, "the rules of res judicata principles would be entirely short circuited." *Travelers Indem. Co.*, 557 U.S. at 137 (citations omitted). Accordingly, if the Court holds that SEC ALJs are inferior officers who were not constitutionally appointed, final SEC judgments should be left intact.

B. Pending Cases Not Yet Final

Where an appointment of an "inferior officer" has been found insufficient in the past, *see e.g., Ryder*, 515 U.S. at 180-188, this Court has found that a subsequent proper appointment or ratification is sufficient for the inferior officer to take future actions. *Edmond v. U.S.*, 520 U.S. 651, 666 (1997).

For administrative determinations that have been properly challenged based on an alleged unconstitutional appointment and are not yet final, the Court should provide clear guidance regarding the ratification or appointment of Administrative Law Judges and the remand for review or rehearing of pending cases by properly appointed ALJs. *See e.g., American Constr. Co. v. Jacksonville, T. & K. W.R. Co.*, 148 U.S. 372, 387 (1893); *United States v. L.A. Tucker Truck Lines*, 344 U.S. 33, 38 (1952); *United States v. American-Foreign S.S. Corp.*, 363 U.S. 685, 691 (1960); *Ryder v. United States*, 515 U.S. 177, 180-88 (1995); *Khanh Phuong Nguyen v. United States*, 539 U.S. 69, 73-74 (2003).

It is anticipated that this decision will impact the more than 1930 current ALJs who are estimated to have well over one million pending cases.[8] A lengthy or complicated process to review or rehear those cases could result in significant delays and increased backlogs.

C. Prospective Cases

For prospective administrative adjudications, FALJC is concerned about the extensive number of administrative cases affecting the public.[9] *See* Appendix D.

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[8] Caseload statistics for current administrative adjudication are not readily available. Administrative Conference of the United States (ACUS) and Stanford Law School compiled some statistics regarding caseloads in administrative adjudication for FY 2013. These statistics did not include all agencies, included cases heard by ALJs as well as other administrative adjudicators, and included cases on appeal within the agency beyond the hearing level. Appendix D compiles the verified hearing level caseload statistics for cases handled by ALJs. For the 18 agencies for which ALJ statistics were available, there were over a million pending cases. Given increasing caseloads and the number of agencies not included, the number of currently pending cases is significantly higher. *See* Appendix D.

[9] A variety of vexing questions remain. If an ALJ was unconstitutionally appointed, but transfers to a different agency and is constitutionally appointed, does the subsequent appointment cure the initial unconstitutional appointment? If an ALJ was constitutionally appointed, but transfers to a different agency, must the ALJ's appointment be ratified by the head of the new agency, notwithstanding prior proper appointment? What if the "Heads of Departments" or a majority thereof, decline to ratify an appointment or reappoint an incumbent ALJ or ALJs for political or other reasons? Do ALJs retain their statutory "only for good cause" protection under the APA in the event the head of an agency constructively removes an ALJ by declining to reappoint them or ratify their prior appointment? Who is responsible for

Congress created many independent agencies, diverse in structure, function, and design, with various indicia of independence, including differing combinations of independent litigation and adjudication authority and for-cause removal restrictions. *See PHH Corp. v. Consumer Fin. Protection Bureau*, 881 F.3d 75 at (D.C. Cir. 2018) (summarizing Court precedent and academic scholarship affirming Congressional design of agencies with various indicia of independence that do not infringe on the President's constitutional duty to ensure that the laws are faithfully executed).

The grant of certiorari is limited to the question of whether the SEC judges are required to be appointed as inferior officers of the United States.[10] Such a

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appointing or ratifying ALJs who are loaned to hear cases for other agencies?

[10] The Court did not grant an expansion of the issue in this case. However if the Court considers the ALJ "for-cause" protection as incident to the Appointments Clause issue, an ALJs' sole adjudicatory function should permit Congress constitutionally under the APA to provide "only for good cause" tenure protection to enhance fairness and procedural due process and to ensure sufficient decisional independence and impartiality, free from agency or Executive pressure that would exist with at-will removal authority. The intent of Congress to provide sufficient ALJ decisional independence and impartiality for the benefit of the public and due process under the APA should be upheld. *See* Jerome Nelson, *Administrative Law Judges' Removal "Only For Cause": Is That Administrative Procedure Act Protection Now Unconstitutional?*, 63 Admin. L. Rev. 401, 416-18 (2011) (concluding that "there is no reason to bring the ALJ's more limited and purely adjudicatory roles closer to presidential removal" and "[s]uch a radical outcome, with a serious adverse impact on the fairness of the administrative adjudicatory system, is not required by [*Free Enterprise Fund v. Public Co. Accounting Oversight Board*, 561 U.S. 477, 493 (2010).]"); *see also* Kent Barnett, *Avoiding Independent Agency Armageddon*, 87 Notre Dame l. Rev. 1349, 1397-99 (2012) (arguing that the particular

determination would substantially impact the administrative adjudication system which relies on over 1900 ALJs to provide due process for the benefit of the public. FALJC suggests that the Court consider the potential impact of this matter on the administrative adjudication system and the benefit the public receives from independent adjudicators in on-the-record proceedings.

Scholars in administrative law have identified concerns and proposed various changes to the administrative adjudication system. However, the intent of Congress through the APA to provide an impartial and independent ALJ oversight check on the limits on executive agency action should be upheld and to the extent any improvements are needed, action to modify the APA should be taken by Congress. *See e.g.*, Barnett, 66 Vand. L. Rev. at 802.[11]

FALJC encourages the Court to insure that ratification of incumbent ALJs is sufficient under the Appointments Clause to permit ALJs to adjudicate existing and future disputes consistent with the Constitution to ensure stability and continuity within administrative adjudication.

CONCLUSION

The resolution of this proceeding should preserve ALJ decisional independence created by Congress in the APA, provide clear guidelines regarding the

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combination of tenure protections for ALJs does not impermissibly interfere with the President's supervisory power).

[11] Congress has considered changes to the current system. H.R. 5177, 106th Cong. 2d Sess. (2000) was introduced in the House of Representatives in 2000. https://www.congress.gov/bill/106th-congress/house-bill/5177/text.

ratification or appointment of ALJs and the review of pending cases by properly-appointed ALJs, and insure that ratification of incumbent ALJs is sufficient under the Appointments Clause to permit ALJs to adjudicate existing and future disputes consistent with the Constitution.

Respectfully submitted,

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February 26, 2018

APPENDIX

APPENDIX A

Federal Administrative Law Judges by agency and level (EHRI-SDM as of March 2017)*

AGENCY	AL-3	AL-2	AL-1	Total
Commodity Futures Trading Commission	0	0	0	0
Consumer Financial Protection Bureau	1	0	0	1
Department of Agriculture	2	1	0	3
Department of Education	2	0	0	2
Department of Health and Human Services/DAB	5	0	0	5
Department of Health and Human Services/FDA	0	0	0	0
Department of Health and Human Services/OMHA	94	6	1	101
Department of Homeland Security/United States Coast Guard	5	1	0	6
Department of Housing and Urban Development	2	0	0	2
Department of the Interior	8	1	0	9
Department of Justice/Drug Enforcement Administration Review	2	0	0	2
Department of Labor	32	8	1	41
Department of Transportation/Office of the Secretary	2	1	0	3
Environmental Protection Agency	2	1	0	3

Federal Communications Commission	1	0	0	1
Federal Energy Regulatory Commission	12	0	1	13
Federal Labor Relations Authority	1	1	0	2
Federal Maritime Commission	2	0	0	2
Federal Mine Safety and Health Review Commission	14	0	1	15
Federal Trade Commission	1	0	0	1
International Trade Commission	6	0	0	6
Merit Systems Protection Board	0	0	0	0
National Labor Relations Board	30	3	1	34
National Transportation Safety Board Commission	3	0	0	3
Office of Financial Institution Adjudication	2	0	0	2
Securities and Exchange Commission	4	1	0	5
Small Business Administration	0	0	0	0
Social Security Administration	1,642	13	0	1,655
United States Postal Service	1	0	0	1
TOTAL	1,888	38	5	1,931

* From: https://www.opm.gov/services-for-agencies/administrative-law-judges/#url=ALJs-by-Agency.

APPENDIX B

THE FEDERAL ADMINISTRATIVE LAW JUDGES CONFERENCE

P.O. Box 1772 • Washington, DC 20013 •
www.faljc.org

MISSION OF THE

FEDERAL ADMINISTRATIVE LAW JUDGES CONFERENCE

Founded February 6, 1947

The purposes of the Conference are to further the public interest by improving the administrative process; to foster faithful, efficient, and effective performance of the functions assigned to Administrative Law Judges under the various statutes governing Federal administrative proceedings; to advance the professional standing, education and welfare of the Administrative Law Judges employed by the Government of the United States; to defend the independence of federal Administrative Law Judges; to defend the protections afforded Administrative Law Judges by the Administrative Procedure Act; and to encourage the cordial and friendly relations among the members of the Conference and with the judiciary, government agencies, and public and private organizations concerned with the administrative process.

LEADERSHIP

The Officers and Executive Committee of FALJC includes Administrative Law Judges from the following agencies:

CFPB	FLRA	OMHA-HHS
DEA	FMC	OSHRC
DOI	FMSHRC	SEC*
DOL	HHS-DAB	SSA
DOT	HUD	USCG
EPA	ITC	USDA
FCC	NLRB	USPS
FERC	NTSB	

* FALJC members employed by the SEC did not participate in discussion about or preparation of this brief.

APPENDIX C

Job Title: Administrative Law Judge Examination*

Job Announcement Number: ALJ2017-847661

HOW YOU WILL BE EVALUATED

Basis for Rating:

After you submit a complete online Application Package and you have cleared the preliminary qualifications screening, you will receive information and an internet link via email announcing the upcoming time period in which you must complete the Situational Judgment Test (SJT), Writing Sample, and Experience Assessment online. If you do not complete the SJT, Writing Sample, and Experience Assessment in the required time period, a Notice of Results (NOR) will be issued to you indicating a rating of "ineligible" and no further action will be taken on your application. See the "Appeals Process" section below.

Online Component: Situational Judgment Test (SJT), Writing Sample, and Experience Assessment

Section 1: SJT - The SJT presents applicants with a set of work-related problems or critical situations and asks applicants to indicate which of the multiple-choice response options they would most likely and least likely take to handle the situations. The SJT is administered online, is timed, and involves text-based scenarios as well as video-based scenarios with closed captioning. Applicants may take as long as they wish to review the instructions but are given 75 minutes to respond to the SJT questions.

Section 2: Writing Sample - The Writing Sample is an exercise in which applicants write a response to a pre-determined topic. Applicants type their writing sample responses online and the exercise is timed.

Applicants may take as long as they wish to review the instructions but are given 35 minutes to prepare a response to the question.

Section 3: Experience Assessment - The Experience Assessment includes multiple-choice and open-ended questions about work experience that is related to ALJ positions.

Applicants select a multiple-choice response and write a narrative response, as appropriate, to indicate and document their experience associated with the targeted competency. The Experience Assessment is not timed.

Applicants who are invited to participate in the SJT, Writing Sample, and Experience Assessment will receive an advance email with specific instructions for completing these assessments and details about computer system requirements. After you have submitted your responses to the online assessments (i.e., SJT, Writing Sample, and Experience Assessment), you will not be allowed to make changes to your submission.

If the score for your performance on the SJT, Writing Sample, and Experience Assessment is within the range for the higher-scored sub-group of all the eligible applicants, you will be invited to participate in the Written Demonstration, Logic-Based Measurement Test, and Structured Interview. You will be notified via email regarding when and where to report for the Written Demonstration, Logic-Based Measurement Test, and for the Structured Interview.

If the score for your performance on the SJT, Writing Sample, and Experience Assessment is not within the range for the higher-scored sub-group of all the eligible applicants, you will be notified via email that you will no longer be considered for this current ALJ

Job Opportunity Announcement. You will not be invited to participate in the Written Demonstration, Logic-Based Measurement Test, and the Structured Interview.

NOTE: In determining the SJT, Writing Sample, and Experience Assessment score, veterans' preference points will be applied to the scores of applicants who are entitled to such points and have submitted the required documentation. For applicants who successfully complete the remaining components of the examination, preference points will then be withdrawn from the SJT, Writing Sample, and Experience Assessment score, so that veterans' preference points, when applied to the applicant's final score for the entire examination, will be counted only once.

Proctored Component: Written Demonstration (WD) and Logic-Based Measurement Test (LBMT). If you are invited to participate in the WD and LBMT, this component of the examination will be administered to you in a proctored environment in two separate sessions on one day, unless informed otherwise.

Section 1: WD - The purpose of the WD is to evaluate an applicant's ability to prepare a clear, concise, and well-reasoned legal decision of the type that one might be expected to write if employed as an ALJ. The WD is scheduled for 5 hours to allow time for instructions and other administrative processes, but actual testing time is 4 hours. The WD is conducted in a proctored environment using a laptop computer provided by OPM, and will be administered in one location in the Washington, DC area.

If you do not receive the required minimum score on the WD, you will not receive a final numerical rating and will not be placed on the ALJ register.

Section 2: LBMT - The LBMT presents applicants with a set of scenarios and multiple- choice response options. Only one response option in each scenario is logically accurate, while the remaining options are logically inaccurate. Applicants are asked to indicate which one response option is logically accurate. OPM will provide writing utensils and a scantron form to document your answers. The LBMT is conducted in a proctored environment and will be scheduled for 2½ hours to allow time for instructions, but actual testing time is approximately 2 hours. The LBMT will be administered in one location in the Washington, DC area.

You must complete the WD and LBMT before participating in the Structured Interview.

In-person Component: Structured Interview (SI). If you are invited to participate in the SI, this part of the examination will be administered in an in-person panel interview environment.

SI - The objective of the SI is to evaluate an applicant's responses to competency-based questions related to being an ALJ. A panel will conduct the interview and evaluate the responses provided by the applicant. The interview will last approximately one hour, but you will need to arrive early to allow time for instructions. The SI will be administered in one location in the Washington, DC area.

If you do not receive the required minimum score on the SI, you will not receive a final numerical rating and will not be placed on the ALJ register.

NOTES:

- **Applicant Expenses:** Travel, lodging and other expenses in association with the ALJ examination are the responsibility of the applicant.
- **Reasonable Accommodations**
  - **ALJ Examination Components:** Refer to the Assessment Questionnaire. All requests must be approved prior to the start of the particular examination component.
  - **In-person Component:** Electronic timing devices (i.e., timer on cell phone, etc.) must be pre-approved. OPM reserves the right to inspect the electronic timing device immediately before the component begins and immediately after the component ends or to provide the applicant with an alternative timing device.
- **Electronic Devices:** Use of electronic devices (e.g. cell phones, watches, etc.), connected to the internet is prohibited while participating in the ALJ examination.
- **Confidentiality Agreement:** If you sign a confidentiality agreement for an examination component, you are bound by the conditions of the agreement and are prohibited from discussing, publishing, or sharing the test questions or test materials with others, regardless of whether or not the others are applicants for the ALJ examination. Violating the terms of the agreement will disqualify you from further participation in the ALJ examination process or placement on the ALJ register of eligibles.

- **Inclement Weather During Proctored and In-Person Components:** Information regarding the inclement weather policy for the Proctored Component (WD/LBMT) and In-Person Component (SI) of the ALJ examination is posted on the OPM ALJ webpage at: https://www.opm.gov/services-for-agencies/administrative-law-judges/#url=Inclement-Weather. Applicants must follow the instructions described in the notice.

Final Numerical Rating: Applicants who complete all portions of the assessment process and achieve the minimum required (passing) score on both the WD and SI will be issued a final numerical rating on a scale of **1 – 100**. The rating will be based on the scores assigned for the SJT/Writing Sample/Experience Assessment, the WD/LBMT, and the SI components of the examination with a maximum possible total score of **100**, excluding veterans' preference. If you do not claim veterans' preference, this earned rating will be your final numerical rating. If you are eligible for veterans' preference (other than on the basis of sole survivorship, as described below) and have submitted the required documentation, 5 or 10 points, as appropriate, will be added to your total earned rating to determine your final numerical rating.

Your official Notice of Results and a notice describing your appeal rights will be issued after OPM completes the administration of the ALJ examination for the entire group of applicants that participated in the examination. Applicants also can check the ALJ page on OPM's website https://www.opm.gov/services-for-agencies/administrative-law-judges/ for information regarding when examination related notices have been released.

Appeals Process:

An ALJ Appeals Panel (Panel) will be convened to adjudicate preliminary qualification appeals before all other ALJ assessment appeals.

All other ALJ assessment appeals (including appeals from ratings indicating the applicant was determined to be 'ineligible' at any stage of the ALJ assessment process, after the preliminary qualifications process) will be adjudicated after all final numerical ratings have been assigned. The Panel will adjudicate such appeals from the following categories of applicants who believe their ratings were assigned in error:

1. An applicant who received a NOR indicating that his/her SJT, Writing Sample (WS), and Experience Assessment (EA) score was not within the range for the higher- scored sub-group of all the eligible applicants and, therefore, did not receive further consideration for this current ALJ Job Opportunity Announcement.
2. An applicant who did not receive a minimum required score on the WD and/or SI, did not receive a final numerical rating, and was not placed on the ALJ register.
3. An applicant who participated in the SJT, WS and EA, the WD/LBMT, and SI components and after further review of his/her bar status does not satisfy the licensure requirement.
4. An applicant who received a NOR with a final numerical rating, for appeal of the entire examination.

The Panel has the authority to **affirm, raise,** or **lower** the rating; change a rating from eligible to ineligible and **remove** an applicant from the register;

or **remand** for further development. An appeal must be filed by email within 30 calendar days from the date of the NOR. We will not accept appeals or clarifying appeals information filed past the 30 calendar day deadline. Appeals are adjudicated based on the record. OPM may obtain confirming or clarifying information from state bar licensing agencies and other official repositories. The decision of the Appeals Panel is final, and exhausts further administrative appeal rights. Additional details regarding the appeal process will be provided after the NORs have been issued to all applicants.

NOTE: If you receive a final numerical rating, and your name is placed on the ALJ register, and you appeal your numerical rating, your name will remain on the register, associated with your original score of record while the appeal is being processed. If, however, you are selected for an ALJ position, your name will be removed from the register and your pending appeal will be cancelled.

Questions regarding the situations below are not subject to the ALJ Appeals Panel adjudication process. Instead, such inquiries are handled through separate administrative review procedures and must be sent to aljapplication@opm.gov.

1. Applicants who did not attend or complete the WD/LBMT or SI Components.
2. Applicants who voluntarily withdrew their application from consideration from the ALJ examination.
3. Denial of a reasonable accommodations request.
4. Veterans' preference adjudication.

5. Applicants who received a NOR indicating suspension from the ALJ register for failure to continuously possess a license to practice law while on the ALJ competitive register and during the selection process or any appeal review.

Retaking the ALJ Examination: You may retake the ALJ examination when the examination is open to the receipt of new applications if:

- You received a NOR indicating any "ineligible" rating at any stage of the ALJ examination assessment process
- You received a final numerical rating before June 2017.

In any of the above situations, you are required to retake all parts of the examination. Please note that once you start retaking the examination, in order to receive a new final numerical rating and remain on the register, you must successfully complete all components of the examination. Your most recent rating will become your new rating of record. This new rating can be higher than, the same as, or lower than the score you received previously, or it can be an ineligible rating.

NOTE: If you reapply for the examination while you have an appeal pending, the reapplication will automatically terminate the appeal. If you have already reapplied for a new iteration of the examination, OPM will not process any subsequent attempt to appeal from an earlier NOR.

If you are a 10-point veterans' preference eligible, you have the right to reopen the ALJ Job Opportunity Announcement at any time after it closes, pursuant to 5 CFR 332.311, to participate in a quarterly

examination. You have this right even if you have received a final numerical rating and your name has been placed on the register. You will, however, be bound by the result of retaking the examination. In other words, once you start retaking the examination, in order to receive a new final numerical rating and remain on the register, you must successfully complete all components of the examination. Your most recent rating will become your new rating of record. This new rating can be higher than, the same as, or lower than the score you received previously, or it can be an ineligible rating.

Receiving Employment Consideration:

If you receive a NOR with a final numerical rating, your name will be placed on the ALJ register. The ALJ register is a list of candidates who are eligible for selection and is used to make referrals to agencies for employment consideration when they have entry level ALJ vacancies to fill. Names are referred in descending rank order, including veterans' preference, based on the duty location of the position(s) to be filled and the geographical preference of candidates. It is the responsibility of the hiring agency to make selections from the list of candidates referred for employment consideration from among the highest three available names, taking into consideration veterans' preference and other civil service rules. If you are appointed to an ALJ position, you will be removed from the register and will no longer receive consideration.

By submitting an ALJ application, you are expressing your interest in and availability for ALJ employment.

- Declination of Job Offers: If you decline two (2) job offers you will be suspended from the ALJ register for a period of one (1) year or until the

register is terminated, whichever comes first. If after one (1) year you wish to have your name returned to the ALJ register, you must submit your request in writing to the ALJ email address at: aljapplication@opm.gov. Your request to end your suspension and have your name returned to the register will be accepted as long as the register on which you were placed has not been terminated, and you meet the licensure requirement.

- Non-Availability or Declination of Employment Consideration for Any Reason: As stated in the Geographic Availability section (see below), *"If after selecting your geographical location(s) you decline consideration for a geographical location(s) for which you indicated availability, you will be removed from further consideration for that location(s). You will not be able to reinstate a location from which you have been removed until the next ALJ Job Opportunity Announcement open period."* If you decline to be considered for any location(s) for which an agency is, at that time, seeking to consider you, you will be removed from further consideration for the location(s). Again, you will not be able to reinstate the location(s) until the next ALJ Job Opportunity Announcement open period.

If you become unavailable for consideration for a period of time, you should request to have your name suspended due to unavailability from the register. Such requests for suspension, as well as requests to end the suspension and have your name restored to the register, must be submitted to aljapplication@opm.gov. Requests to end the suspension and have your name restored to the register will be accepted as

long as the register on which you were placed has not been terminated, and you meet the licensure requirement. OPM may extend the expiration date of the register at any time. Prior to the expiration date, applicants on the register will be notified regarding their status and any action impacting their eligibility.

If your name is referred for consideration from the register, and you fail to respond to an inquiry from the prospective employing agency, you will be considered unavailable for appointment, and your name will be suspended from the ALJ register due to unavailability until you request to have your name restored to the register as described in the preceding paragraph.

* OPM 2017 guidance.

APPENDIX D

Adjudication Research
Caseload Statistics, FY 2013
Verified Administrative Law Judge Cases*

Joint project of the Administrative Conference of the United States and Stanford Law School

Agency	Office	Total # Cases Filed/ Opened FY2013	Total # Cases Decided/ Closed FY2013	Total # Cases Pending (End FY2013)
Social Security Administration	Office of the Chief Administrative Law Judge	826,635	793,580	847,984
Department of Health and Human Services	Office of Medicare Hearings and Appeals	384,151	79,377	240,116
Federal Mine Safety and Health Review Commission	Office of Administrative Law Judges	6,898	12,262	7,612
Department of Labor	Office of Administrative Law Judges (OALJ)	4,269	3,534	5,004
Department of Labor	Board of Alien Labor Certification Appeals (BALCA)	3,621	2,215	5,222

Occupational Safety & Health Review Commission	Office of the Chief Administrative Law Judge	2,215	2,460	909
National Labor Relations Board	Division of Judges	1,292	707	352
Department of Labor	Office of Administrative Law Judges	556	519	552
National Transportation Safety Board	Office of Administrative Law Judges	311	308	3
Federal Labor Relations Authority	Office of Administrative Law Judges	271	266	122
Environmental Protection Agency	Office of Administrative Law Judges	46	25	24
United States International Trade Commission	Office of the Administrative Law Judges	39	62	41
Department of Commerce	HUD Office of Administrative Law Judges	10	3	7
Federal Maritime Commission	Office of Administrative Law Judges	9	14	9
Department of the Treasury	Office of Administrative Law Judges	5	2	3

Federal Trade Commission	Office of Administrative Law Judges	5	5	2
Department of Commerce	United States Coast Guard Office of Administrative Law Judges	3	1	2
Consumer Financial Protection Bureau	Office of Administrative Adjudication	1	0	1
TOTALS		1,230,337	895,340	1,107,965

* Caseload statistics, edited to include only hearing level cases from Administrative Law Judge offices with verified numbers. Original data available at: https://acus.law.stanford.edu/reports/caseload-statistics.

These are the most recent and most accurate statistics publicly available. It is noted that statistics from only 18 of the more than 30 agencies using ALJs are included. In addition, caseloads are increasing. For example, at HHS/OMHA, as of June 2, 2017, there were 607,402 pending ALJ cases and "[o]n its current course, the backlog is projected to grow to 950,520 by the end of fiscal year 2021." *AHA v. Price*, 867 F.3d 160, 163 (D.C. Cir. 2017).

Given increasing caseloads and the number of agencies not included, the number of currently pending cases is significantly higher.

No. 17-130

In the Supreme Court of the United States

RAYMOND J. LUCIA,
and RAYMOND J. LUCIA COMPANIES, INC.,
Petitioners,

–v–

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF AMICUS CURIAE THE FORUM OF UNITED STATES ADMINISTRATIVE LAW JUDGES IN SUPPORT OF NEITHER PARTY

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SUPREME COURT PRESS • (888) 958-5705 • BOSTON, MASSACHUSETTS

QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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Continental Congress 1774-1789, at 626 (Gaillard Hunt ed., 1914). And the Minutes from a February 1778 session of the Continental Congress described continental-level civil and military officers as "officer[s] of the United States." Minutes of Feb. 9, 1778, *in* 10 *Journals of the Continental Congress*, *supra*, at 138-40 (Worthington Chauncey Ford ed., 1908); *see also generally Officers*, *supra*, at 475-79 (providing more in-depth explanation of evidence from the *Journals of the Continental Congress* and Series I of the Readex Early American Newspapers database containing 340,000 newspaper issues from 1690 to 1876).

In addition, on a number of occasions the Founders used a variety of distinct phrases to describe Article II officers—suggesting that the descriptor "Officers of the United States" was not considered a precise term of art. *See Officers*, *supra*, at 474. For example, Alexander Hamilton in Federalist No. 77 discussed removal and appointment procedures for "officers of the government," the Anti-Federalist essayist writing as "The Federal Farmer" described Article II officers as "officers of the union," and Representative Roger Sherman used the phrases "officers of the United States" and "officers of the Federal Government" interchangeably during a 1790 congressional debate on militia legislation. *See* The Federalist No. 77, at 396; The Federal Farmer, Anti-Federalist No. 76-77: An Anti-Federalist View of the Appointing Power Under the Constitution (1788), *in The Anti-Federalist Papers*, *supra*, at 293, 294 (Bill Bailey ed., n.d.), https://perma.cc/XM7Q-XV4B; 14 *Documentary History of the First Federal Congress of the United States of America, 4 March 1789-3 March 1791*, at 120-21 (William Charles diGiacomantonio et al. eds., 1995).

Also, examination of every use of the phrase "officers of the United States" in the drafting and ratification debates, the Federalist Papers, and the Borden collection of Anti-Federalist essays revealed no direct definition of the precise scope of the phrase. *See Officers*, *supra*, at 468 & n.131, 474-75. *But see id.* at 475 & n.164 (noting one contradictory use of the phrase during the first congressional debates). This may be because the term "officer" had a "common and known acceptation" at the time. *See* 4 *The Debates in the Several State Conventions, on the Adoption of the Federal Constitution* 454-55 (Jonathan Elliot ed., Washington, Jonathan Elliot 2d ed. 1836) (hereinafter *Elliot's Debates*) (recording an 1806 congressional debate statement); *see also* 8 *Annals of Cong.* 2294, 2306 (1799) (recording Rep. Harper's reference to the "universally received signification of the term 'office'").

C. Founding-era dictionaries and commentaries

Because the phrase "Officers of the United States" is not a term of art for especially important officials, it makes sense to turn to the late eighteenth century meaning of the standalone term "officer" to determine the scope of federal officials under the Appointments Clause.

The majority of the ten Founding-era dictionaries that *amicus* surveyed defined a civil "officer" to be a "man employed by the public(k)" and described an "office" as a "public employment" or a "public charge." *See, e.g.*, 2 Samuel Johnson, *A Dictionary of the English Language* (London, J.F. & C. Rivington 6th ed. 1785) ("Officer": "1. A man employed by the publick"; "2. A commander in the army;" "3. One who has the power

of apprehending criminals, or man accountable to the law"); *see also Officers*, *supra*, at 486-88 (cataloguing the dictionary definitions). The only one of the ten Founding-era dictionaries with a materially different definition explained that the word "officer" "in general signifies any person that has a peculiar post or business appointed him." *See* Thomas Dyche & William Pardon, *A New General English Dictionary* (London, Toplis & Bunney 18th ed. 1781); *Officers*, *supra*, at 486 & n.226. Chief Justice Marshall recounted a similar definition several decades later in an 1823 circuit court opinion, explaining: "An office is defined to be 'a public charge or employment,' and he who performs the duties of the office, is an officer. If employed on the part of the United States, he is an officer of the United States." *United States v. Maurice*, 26 F. Cas. 1211, 1214 (C.C.D. Va. 1823) (No. 15,747); *see also* Noah Webster, *An American Dictionary of the English Language* (New York, S. Converse 1828) ("officer": a "person commissioned or authorized to perform any public duty").

The ordinary-language dictionary definitions and Chief Justice Marshall's explanation are consistent with eighteenth century legal dictionary definitions of "officer," which similarly incorporate the concept of a public charge or duty. *See Officers*, *supra*, at 488-90. For example, Matthew Bacon states that "the Word Officium principally implies a Duty, and ... the Charge of such Duty." 3 Matthew Bacon, *A New Abridgment of the Law* *718-19 (London, C. Bathurst 4th ed. 1778). He then observes that officer status is not dependent on the significance or level of importance of one's duty: An officer "is not the less a Public Officer, where his Authority is confined to narrow Limits; because it is the Duty of his Office, and the Nature of that Duty,

which makes him a Public Officer, and not the Extent of his Authority." *Id.* at *719. Further underscoring that one's eighteenth century status as an "officer" was unrelated to discretion or final decisionmaking, Bacon also describes a class of "Ministerial Offices." *See id.* This group included positions like the "Office of Register of Policies of Assurance," which "required only the Skill of Writing after a Copy," and recordkeepers like chirographers who kept records of court-imposed fines. *See id.* at *734; Dyche & Pardon, *supra* (defining "Chirographer").

The bestselling eighteenth century dictionary by Nathan Bailey used the words "officer(s)" and "office(s)" more than 500 times to define other terms. *See Officers, supra*, at 485 (discussing the "officer" and "office" references); Gregory E. Maggs, *A Concise Guide to Using Dictionaries from the Founding Era to Determine the Original Meaning of the Constitution*, 82 Geo. Wash. L. Rev. 358, 361, 367-81 (2014) (discussing Bailey's dictionary). Treating Bailey's dictionary as a self-contained corpus, *amicus* examined the context of each of those references. *See Officers, supra*, at 485. The dictionary characterized as "officers" numerous assistants, recordkeepers, and other public officials engaged in menial tasks. *See id.* at 490; *see generally* N. Bailey, *An Universal Etymological English Dictionary* (London, J. Murray 25th ed. 1783).

For example, "Messengers [of the Exchequer]" were "officers belonging to that Court, who attend the Lord Treasurer, and carry his letters and orders." Bailey, *supra*, (*Messengers*). A sword-bearer was "an officer who carries the sword of state before a magistrate." *See id.* (*Sword*). Satellites were "Life-Guards, or Officers attending upon a Prince." *Id.* (*Satellites*). A "Swabber" was

"an inferior officer on board a ship of war, whose office it is to take care that the ship be kept clean." *Id.* (*Swabber*). A "sewer" was "an officer who comes in before the meat for a King or Nobleman, and places it upon the table." *Id.* (*Sewer*). A "Gauger" was "an officer employed in gaging," or measuring the contents of a vessel. *Id.* (*Gager/Gauger*; *Gage/Gauge*). A Chafe-Wax was "an Officer belonging to the Lord Chancellor, who fits the wax for [the] sealing of writs." *Id.* (*Chafe*). An "Assay-Master" was "an officer of the Mint, who weighs the bullion, and takes care that it be according to the national standard." *Id.* (*Assay*). And a butler was "an officer that provides the king's wines." *Id.* (*Botiler/Butler*). *See also Officers*, *supra*, at 490-94 (detailing a lengthier list).

The dictionary's characterization of these officials as "officers" would have influenced the late eighteenth century American understanding of the term even though the new constitutional system embraced few of these specific positions. *See Officers*, *supra*, at 492. *But see* Act of Aug. 4, 1790, ch. 5, § 6, 1 Stat. 145, 154 (1790) (repealed 1799) (providing for gaugers); Act of Apr. 2, 1792, ch. 16, § 1, 1 Stat. 246, 246 (1792) (providing for an Assayer). The Framers intentionally rejected the British approach for creating offices and appointing officers, but no evidence suggests the Constitution imported an altered meaning of the word "officer" itself. *See Officers*, *supra*, at 493-94. One complaint underlying the colonists' war for independence was that the King had "erected a multitude of New Offices, and sent hither swarms of Officers to harrass our people." *The Declaration of Independence* para. 12 (U.S. 1776). Under British practice the King had power to both create and fill public offices. *See* The Federalist No. 69, at 360-61 (A. Hamilton); *Officers*, *supra*, at 492-

93 (further describing British practice). The Framers rejected this potential for abuse, cleanly separating the power to create offices from the power to appoint officers to fill them. *See* Mascott, *Constitutionally Conforming Agency Adjudication*, *supra*, at 28; Volokh, *supra*, at 769. The Court should not acquiesce in resisting this safeguard by ratifying the lower courts' expansive creation of a non-officer "employee" class free from separation-of-powers limits that preserve accountable and transparent governance.

D. Contextual uses of "Officer" and "Officers of the United States" in Founding-era sources debating the Constitution

The Federalist Papers, the Borden collection of Anti-Federalist essays, and the drafting debates contain hundreds of references to the terms "officer(s)" and "office(s)." *See Officers*, *supra*, at 468 n.131. Examining their context, as well as every reference to "Officers of the United States" in the ratification debates, strongly suggests that "officer" had a very broad scope in the late eighteenth century. *See Officers*, *supra*, at 494-504 (detailing this analysis and explaining any potential counter-examples). The Framers and ratifiers believed that thousands of officials would qualify as "officers." In fact, their statements do not appear to account for any class of ongoing non-officer positions other than a class of "servants" and "attendants." *See Officers*, *supra*, at 450, 503; *see also, e.g.*, Federal Farmer XVIII, *supra*, *in The Anti-Federalist Papers*, *supra*, at 162 (referring to the parties who would work in the capital city as the federal government's "own members, officers, and servants").

Following are several illustrative examples. During the North Carolina ratification debate, Mr. Maclaine described "inferior officers of the United States" as "petty officers" who maintained "trifling" duties. 4 *Elliot's Debates*, *supra*, at 43-44; *see also Officers*, *supra*, at 496-97. Mr. Taylor observed that if the Constitution were adopted, "we shall have a large number of officers in North Carolina under the appointment of Congress" because, for example, there would be "a great number of tax-gatherers." *See* 4 *Elliot's Debates*, *supra*, at 36. During the drafting debates, Gouverneur Morris observed that the executive would have the duty to appoint "ministeral officers of the administration of public affairs." 2 *Farrand's Records*, *supra*, at 52. Later in the drafting process, James Wilson observed that the appointing power would encompass even "tide-waiter[s]," a position that Samuel Johnson's dictionary described as an "officer who watches the landing of goods at the customhouse." *See* Johnson, *supra* (*Tidewaiter*).

The Anti-Federalist essayist known as the "Federal Farmer" expressed concern that federal taxation powers would lead to "many thousand officers solely created by, and dependent upon the union." The Federal Farmer, Anti-Federalist No. 41-43 (Part I): The Quantity of Power the Union Must Possess Is One Thing; The Mode of Exercising the Powers Given is Quite a Different Consideration (1788), *in The Anti-Federalist Papers*, *supra*, at 148, 149. James Madison disagreed and believed the federal government would have relatively few officers. *See Officers*, *supra*, at 501-02 (discussing these various positions). But this is because Madison believed that the federal government's "few and defined" powers would require it to have only one officer for every "thirty or forty, or even more, officers" in

the states, which had "numerous and indefinite" powers. The Federalist No. 45, at 241. In particular, Madison concluded that state officers would exceed federal officers "beyond all proportion, both in number and influence," *see id.* at 240, because he believed that state officers would collect taxes on behalf of the federal government if it ever imposed a federal internal revenue tax, *see id.* at 241.

Madison clearly believed, however, that the term "officer" itself had a broad scope, embracing many officials. *See Officers*, *supra*, at 502. In describing state and local officers, he referred to "the justices of peace, officers of militia, ministerial officers of justice, with all the county, corporation, and town officers ... having particular acquaintance with every class and circle of people." *See* The Federalist No. 45, at 240. Tellingly, despite the strong disagreements between Federalists and Anti-Federalists over whether the Constitution permitted too strong a concentration of centralized power, writers on both sides shared the same understanding of the broad meaning of the term "officer."

This understanding of "officer" also extended back to the time of the Continental Congress. *See generally Officers*, *supra*, at 537-45. For example, a 1778 resolution regarding military hospitals characterized "apothecaries, mates, stewards, [and] matrons" as "officers." *See* Minutes of Feb. 6, 1778, *in* 10 *Journals of the Continental Congress*, *supra*, at 127, 130 (Worthington Chauncey Ford ed., 1908). These individuals had nondiscretionary duties far below the level that contemporary courts have considered mandatory for "officer" status. A 1775 Continental Congress committee report indicated that the role of mates and apothecaries was to "visit and attend

the sick." *See* Minutes of July 27, 1775, *in* 2 *Journals of the Continental Congress*, *supra*, at 210. The 1775 report also characterized clerks and storekeepers as "officers," observing that storekeepers were "[t]o receive and deliver the bedding and other necessaries by order of the [hospital] director" and clerks were "[t]o keep accounts for the director and store keepers." *See id.* at 210-11 (discussing "the choice of officers"). *But see Officers*, *supra*, at 539-40, 542 & nn.589, 599 (explaining that the actual appointment methods used to fill a number of these positions appeared to be in some tension with the description of them as "office[s]").

Several Continental Congress-Era handwritten lists of "officers" on file at the National Archives also suggest that officials with relatively insignificant responsibilities were considered officers at that time. *See Officers*, *supra*, at 540-41. A 1783 document titled "A List of the Officers" listed positions as low-level as clerk and clerk/interpreter. *See* A List of the Officers in the Department of Foreign Affairs and Their Appointments (1783), *microformed on* Microcopy No. 247, Roll 22 (Nat'l Archives & Records Serv.). A 1775-76 document titled "Officers appointed" listed an engineer, a storekeeper, and a surgeon along with colonels, majors, and brigadier generals. *See* Officers Appointed (n.d.), *microformed on* Microcopy No. 247, Roll 195, Item No. 178 (Nat'l Archives & Records Serv.). The reference to just "officers" in the titles of these two records appears deliberate as several other archives records instead used the label "officers & c." when listing lower-level non-officers like messengers. *See Officers*, *supra*, at 540-41; *see also id.* at 513-15 (explaining that Founding-era messengers and office-keepers likely were not considered "officers" because their responsibilities did not include any governmental tasks imposed by law).

E. Early appointment practices

Early appointment practices during the First Congress confirm the understanding of Article II "officers" as officials responsible for an ongoing statutory duty. The only categories of civil executive officials in ongoing positions cleanly excluded from Article II appointment practices were "(i) positions more like those of 'servants' or 'attendants' and (ii) 'deputies' acting as agents in place of an officer, where the officer was subject to personal legal liability for the deputy's actions."[3] *Officers*, *supra*, at 450.

Clerks maintaining legislatively required records were appointed by department heads in conformity with Article II. *See, e.g.*, Act of Sept. 11, 1789, § 2, 1 Stat. 67, 68 (authorizing the heads of the three executive departments to appoint clerks); *see also Officers*, *supra*, at 508, 511-15. Officials as varied as internal revenue inspectors and supervisors, lighthouse keepers and superintendents, ship masters and first, second, and third mates on revenue cutters (although not "mariners" and "boys"), customs collectors, naval officers, and surveyors also were selected in compliance with the Appointments Clause. *See Officers*, *supra*, at 507-37 (further discussing the First Congress's appointment practices). *But see id.* (noting possible counter-examples like certain officials in

3. These deputy marshals, collectors, surveyors, and naval officers constituted a relatively small category who carried out the duties of their primary officer as his representative. Consequently, they were not considered officers in their own right. *See id.* at 509, 515-20. Other early-level positions bearing the moniker "deputy" were appointed in compliance with Article II where they did not have the same agent-principal liability relationship with a higher-level officer. *See id.* at 520-22 (discussing, among other positions, deputy apothecary generals charged with safekeeping medical equipment and deputy postmasters).

the Territories, *id.* at 528 n.508, and the National Bank, *id.* at 531). Contrary to the suggestion of some modern judicial opinions that Congress can determine "officer" status based on whether it chooses to directly tie statutory duties to a particular official, *see, e.g.*, *Landry*, 204 F.3d at 1133, the original meaning of "officer" encompassed every official who happened to carry out a statutory task—whether Congress had explicitly assigned it to them or not. For example, clerks who kept statutory records were considered "officers" even where statutes just generally required executive recordkeeping without assigning clerks to the job. *See Officers*, *supra*, at 507-08, 513-15. Analogously, today if Congress were to authorize an agency to promulgate rules, every official participating in that task would be an "officer" under the statutory duty standard.

In contrast, messengers and office-keepers did not carry out legislative tasks authorized or required by Congress, so they were not "officers" and Congress consequently did not need to establish their positions "by Law." *See* U.S. Const. art. II, § 2 (requiring that Congress establish the appointments for officers "by Law"). Individuals in these positions served more as assistants and carried out nonstatutorily required tasks like "arranging and preserving the newspapers, and the printed copies of the laws and documents of Congress," as well as "putting up and packing despatches and other papers for transmission by mail." *See* Louis McLane, The Following Arrangement of the Gentlemen Employed, the Distribution of Their Duties, and Rules for Their Performance, Are Directed to be Observed in the Department of State, from and After the 30th June, 1833 (1833), *microformed on* M800, Roll 1, Vol. 1A (Nat'l Archives & Records Serv.).

In apparent contrast to the clerk/messenger dividing line, one set of positions that at least initially did not conform with the statutory-duty "officer" construct is lower-level customs officials like weighers, measurers, gaugers, and inspectors. *See Officers*, *supra*, at 523-27. Numerous Founding-era writings described them as "officers," but they were not selected in compliance with the Appointments Clause in 1789. They were instead subject to hiring by customs collectors who did not head a department. *Compare, e.g.*, Letter from Nathaniel Smith to George Washington (July 10, 1789), *in* 3 The Papers of George Washington 176 (Dorothy Twohig ed., 1989) (requesting to be considered for the "office" of gauger), and Notes on the Collection Bill (HR-11) (n.d.), *in* 16 *Documentary History of the First Federal Congress, 4 March 1789-3 March 1791*, at 1052 (Charlene Bangs Bickford et al. eds., 2004) (describing an inspector as an "officer" in notes on draft legislation), *with* Act of July 31, 1789, ch. 5, § 5, 1 Stat. 29, 36-37 (repealed 1790) (authorizing appointment by collectors); *see also Officers*, *supra*, at 523-27. But Congress addressed this situation in 1799, requiring the "approbation" of the Secretary of the Treasury for the appointment of these customs officials. *See* Act of Mar. 2, 1799, ch. 22, § 21, 1 Stat. 627, 642 (amended 1811). And, an Attorney General opinion issued in 1843 concluded that customs inspectors are Article II officers, observing that any statute permitting customs collectors to appoint inspectors would be "null and void under the constitution." *See* Appointment & Removal of Inspectors of Customs, 4 Op. Att'y Gen. 162, 164-65 (1843).

Measurers, gaugers, and weighers carried out the statutory duties of measuring imported goods for the purposes of calculating customs duties. *See* Tariff Act of 1789, ch. 2, § 1, 1 Stat. 24, 24-26 (repealed 1790); Act of Aug.

4, 1790, § 53, 1 Stat. 145, 172 (repealed 1799). Inspectors carried out the statutory duties of preventing ships from unloading goods without a permit and searching ships suspected of smuggling. *See* Act of Aug. 4, 1790, §§ 30-31, 1 Stat. at 164-65; *Officers*, *supra*, at 524 & n.178. Perhaps Congress did not initially provide for these positions by statute because their payment-for-service compensation structures mimicked aspects of non-officer government contracting positions, a category involving irregular government work existing at the time of the Founding just like today. *See* Act of Aug. 4, 1790, § 53, 1 Stat. at 172 (providing for payment in accordance with the amount of goods measured); *Officers*, *supra*, at 534-37. *But see* Nicholas R. Parrillo, *Against the Profit Motive: The Salary Revolution in American Government* 1-48 (2013) (explaining that fees for services were a routine compensation mechanism for many governmental officials in the eighteenth century).

III. The Court should not distort the meaning of the Appointments Clause based on alleged practical implementation concerns.

In its decision here, the D.C. Circuit suggested that keeping ALJs from the reach of the Appointments Clause is a necessary protection to maintain independence in agency adjudicative proceedings. *See Lucia*, 832 F.3d at 288-89 (discussing "independence" through "tenure and compensation" and declining to "cast aside a carefully devised scheme" by concluding that ALJs are "officers"). But when considering the Appointments Clause in *Buckley*, this Court clearly instructed that practical fears such as the potential partiality of government decisionmakers "do not by themselves warrant a distortion of the Framers' work." *See* 424 U.S. at 134 (refusing to

reject constitutional appointment requirements based on the fear that presidential appointment would unduly influence federal election commissioners who administer presidential campaign rules).

In any event, the politically appointed SEC Commissioners have the last word on whether an ALJ's initial decision stands as the agency's final determination, or whether the Commissioners will instead review the decision. *See* 15 U.S.C. § 78d-1(b). *But see id.* (giving a party a right to Commission review in certain circumstances). When choosing to review, the SEC may consider the matter de novo. *See Lucia*, 832 F.3d at 286. Further, the SEC Commissioners have statutory authority to adjudicate matters in the first instance if they so choose. *See* 15 U.S.C. § 78d-1(a).

To be sure, an ALJ's initial determination, as a practical matter, often is the last word from the agency in adjudication. *See* 15 U.S.C. § 78d-1(c) (providing for ALJ decisions to be deemed "the action of the Commission" if there is no review). And when presiding over cases, ALJs have the power to take final action with respect to many matters that impact private rights like issuing subpoenas and ruling on offers of proof. *See* 17 C.F.R. § 200.14(a). But at the end of the day, whether ALJs meet a theoretical non-Article III standard of independence is immaterial in the sense that the politically appointed *Commissioners* have the final say over adjudication. If this Court believes that democratically accountable, constitutional appointment of adjudicative officials raises independence concerns, the Court should revisit the proper scope of matters that can be resolved by non-Article III adjudication in the first place. *See Stern v. Marshall*, 564 U.S. 462, 482-83 (2011); *see also* Mascott, *Constitutionally Conforming Agency Adjudication*, *supra*, at 42-51. The Court should not

compound any potential concerns over agency adjudicators lacking impartiality and improperly exercising judicial power with the additional error of insulating executive branch adjudicators from the Appointments Clause.

The Framers instituted the Appointments Clause as the mechanism to ensure excellence in government service and democratic accountability in the exercise of government power. *See Freytag*, 501 U.S. at 883-84. Permitting agency staff to hire ALJs enables department heads to distance themselves from public responsibility for adjudicative decisions issued from their agency. *Cf. Free Enterprise Fund*, 561 U.S. at 497-98 (tying public accountability to "a clear and effective chain of command"). Commissioners and department heads have the *power* to issue adjudicative decisions in line with their priorities. They should also bear the public *responsibility*—and, if necessary, the blame—for decisions issued by adjudicators appointed under their headship.

If this Court concludes consistent with Article II's original meaning that ALJs are "officers," aspects of the competitive-based selection of ALJs may remain permissible, at least in some form. *See Officers*, *supra*, at 550-56 (explaining potential constitutional concerns with aspects of the competitive service system as currently structured). Article II assigns Congress the power of establishing offices "by Law." U.S. Const. art. II, § 2, cl. 2. Since the Founding, that power to create offices has been interpreted to carry with it the authority to stipulate at least some credentials that must be held by the inferior officers filling those posts. *See, e.g.*, Volokh, *supra*, at 747; *Officers*, *supra*, at 551; *see also* Edward S. Corwin, *The President: Office and Powers, 1787-1948; History and Analysis of Practice and Opinion* 88-89 (3d ed. 1948).

These issues are multi-faceted and should be further briefed and vetted in an appropriate case. Here, a finding that the SEC's ALJs are "Officers of the United States" under the historical "statutory duty" standard—and thus, department head appointment is required—would answer the appointments-related aspect of the specific question presented to the Court.

CONCLUSION

For the reasons stated, this Court should reverse the D.C. Circuit's judgment.

Respectfully submitted,

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In The Supreme Court of the United States

RAYMOND J. LUCIA AND
RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

BRIEF FOR NATIONAL BLACK LUNG ASSOCIATION AS *AMICUS CURIAE* SUPPORTING AFFIRMANCE

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INTEREST OF *AMICUS CURIAE*[1]

This brief is presented on behalf of the National Black Lung Association. The National Black Lung Association is an organization of coal miners and friends and families of miners who advocate for education, treatment standards, and policy protections for miners who have suffered permanent disability or death as a result of exposure to coal dust.

This court granted certiorari on the question of whether administrative law judges (ALJs) of the Securities and Exchange Commission (SEC) are "officers of United States" within the meaning of the Appointments Clause. *Lucia v. SEC*, 868 F.3d 1021 (D.C. Cir. 2017), *cert. granted*, 2018 WL 386565 (U.S. Jan. 12, 2018) (No. 17-130). Resolution of the question presented is important to the National Black Lung Association because of the integral role that ALJs play in the adjudication of claims under the Black Lung Benefits Act, 30 U.S.C. §§ 901-44.

SUMMARY OF ARGUMENT

If the Court finds a constitutional violation in this case, the Court's remedial determination could

[1] Pursuant to Sup. Ct. R. 37.6, *amicus curiae* and its counsel state that none of the parties to this case nor their counsel authored this brief in whole or in part, and that no person or entity made a monetary contribution specifically for the preparation or submission of this brief. *Amicus curiae* files this brief with the written consent of all parties, copies of which are on file in the Clerk's Office.

dramatically affect coal miners disabled by black lung and their widows. ALJs within the Department of Labor are the primary adjudicators in the black lung benefits system. At a time when black lung disease is resurgent, the Department of Labor's Office of Administrative Law Judges is severely backlogged with claimants waiting years for routine decisions. If the Court were to hold that past decisions by ALJs are void, this could require hundreds of remands back to the agency's Office of Administrative Law Judges, hobbling efforts to address the backlog and leaving vulnerable miners and their families who depend on such benefits.

With the question pending before this Court of the constitutionality of the appointments of ALJs, in December 2017, Secretary of Labor Alexander Acosta ratified the Department of Labor's prior appointments of its ALJs. The letters of ratification were "intended to address any claim that administrative proceedings pending before, or presided over by, administrative law judges of the U.S. Department of Labor violate the Appointments Clause of the U.S. Constitution."[2]

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[2] *See* U.S. Dep't of Labor, OALJ, *Home Page*, https://www.oalj.dol.gov/ (last visited Mar. 29, 2018) ("[T]he Secretary of Labor, R. Alexander Acosta, in his capacity as head of the Department of Labor, ratified the appointment of Chief Judge Stephen R. Henley on December 15, 2017 and of all other Department of Labor ALJs on December 21, 2017. The ratifications were effective immediately.").

The Court should ensure that its holding in this case does not affect existing ALJ decisions in black lung benefits claims.

ARGUMENT

I. Rates of black lung disease, an incurable condition that affects coal miners, are on the rise.

The Federal Coal Mine Health and Safety Act (Coal Act) of 1969 established, among other protections for coal miners, a federal compensation program for those miners disabled or killed by black lung disease, and their surviving dependents. 30 U.S.C. § 901(a).

Black lung disease is a term used to identify collectively a number of breathing diseases caused by overexposure to coal mine dust. Black lung disease is incurable and progresses long after exposure to coal dust ends. Treatment serves solely to alleviate symptoms and prevent complications that may arise. The disease is known to lead to lung impairment, disability, and premature death.[3]

While black lung disease sounds to many like an archaic condition with little relevance in the 21st Century, rates of black lung disease are on the rise, most

[3] U.S. Dep't of Labor, Office of Inspector General, Office of Audit, 05-17-003-01-060, *Effect of OALJ Staffing Levels on the Black Lung Case Backlog* 2 (2017), *available at* https://www.oig.dol.gov/public/reports/oa/2017/05-17-003-01-060.pdf [hereinafter *2017 OIG Report*].

acutely in the Central Appalachian coalfields.[4] Rates of severe black lung disease among career Appalachian coal miners are actually higher now than just after the Coal Act's passage in 1969 when data started being kept.[5]

II. Coal miners and widows applying for black lung benefits typically endure years-long delays due to a backlog before ALJs.

Delays in the federal black lung benefits program are one of the most prominent problems facing coal miners with black lung and their widows.[6]

The federal black lung benefits program is administered by the U.S. Department of Labor. A miner or widow seeking benefits begins the years-long process by submitting a claim to the Department of Labor's Office of Workers' Compensation Programs (OWCP). The most recent publicly available data shows that OWCP takes an average of 235 days to issue a decision.[7]

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[4] Carrie Arnold, *A Scourge Returns: Black Lung in Appalachia*, 124 ENVTL. HEALTH PERSPS. A13 (2016), *available at* http://ehp.niehs.nih.gov/wp-content/uploads/124/1/ehp.124-A13.alt.pdf.

[5] *See* David J. Blackley et al., *Resurgence of Progressive Massive Fibrosis in Coal Miners – Eastern Kentucky, 2016*, 65 MORBIDITY & MORTALITY WKLY. REP. 1385, 1387 (2016), *available at* https://www.cdc.gov/mmwr/volumes/65/wr/pdfs/mm6549a1.pdf.

[6] Evan Barret Smith, *Black Lung in the 21st Century: Disease, Law, & Policy*, 120 W. VA. L. REV. (forthcoming April 2018), *available at* https://ssrn.com/abstract=3152733.

[7] U.S. Dep't of Labor, Office of Inspector General, Office of Audit, 05-15-001-50-598, *Procedural Changes Could Reduce the*

Once OWCP issues its decision, either the claimant or the coal company that would be responsible for benefits may request a formal hearing before an ALJ from the Department of Labor's Office of Administrative Law Judges (OALJ). The ALJ conducts a *de novo* review of the evidence.[8] In 2017, from a sample of 41 black lung cases audited by the Office of the Inspector General, OALJ took an average of 640 days to issue a decision. In one instance, a case remained pending with the OALJ for more than four and a half years.[9]

Parties may appeal an ALJ decision to the Department of Labor's Benefits Review Board. On average, claims remain pending before the Board for 328 days.[10] Either party may appeal decisions from the Board directly to the U.S. Court of Appeals, and then to the U.S. Supreme Court (although the Court has not granted certiorari in a black lung benefits case since 1994).[11] If a court, the Board, or an ALJ identifies an error,

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Time Required to Adjudicate Federal Black Lung Benefits Claims 5 (2015), *available at* https://www.oig.dol.gov/public/reports/oa/2015/05-15-001-50-598.pdf (FY2014 data) [hereinafter *2015 OIG Report*].

[8] U.S. Gov't Accountability Office, GAO-10-7, *Black Lung Benefits Program: Administrative and Structural Changes Could Improve Miners' Ability to Pursue Claims* 7-8 (2009), *available at* https://www.gao.gov/assets/300/297807.pdf [hereinafter *GAO Report*].

[9] *2017 OIG Report* at 3.

[10] *2015 OIG Report* at 5.

[11] *See Director, OWCP v. Greenwich Collieries*, 512 U.S. 267 (1994).

the claim may be remanded. This results in additional years of litigation.

Between 2001 and 2008, in 24% of cases where miners eventually received benefits from their employers, those miners were forced to wait three to six years before benefits were awarded. In 4% of cases, miners were forced to wait six years or more for an award of benefits.[12] Part of the delay in benefits awards stems from the frequency of appeals. In Fiscal Year (FY) 2008, in cases where the OWCP ruled in favor of a miner or widow, coal operators appealed to the OALJ 80% of the time. Additionally, between FY 2004 and FY 2008, approximately 43% of all claims decided by OALJ were appealed to the Board, and about 10% of Board decisions were appealed to the federal appellate courts.[13]

Contributing to the excessive delays that claimants endure, under the Black Lung Benefits Act's broad "modification" procedure, coal operators may reopen final awards. *See* 33 U.S.C. § 922 *incorporated by reference into* 30 U.S.C. § 932(a); 20 C.F.R. § 725.310; *see also Metropolitan Stevedore Co. v. Rambo*, 515 U.S. 291, 294-98 (1995) (holding that § 922 modification is not limited to "particular kinds of factual errors or to cases involving new evidence or changed circumstances" but rather can be used whenever there is a

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[12] These numbers fail to account for claims made by widows, denied claims, and all awards from the Black Lung Disability Trust Fund.

[13] *GAO Report* at 14-15.

change in the conditions "that entitled the employee to benefits in the first place"). These proceedings may be initiated "any time prior to one year after the date of the last payment of compensation." 33 U.S.C. § 922. Modification proceedings start the process over at OWCP and pile years onto the already lengthy process. For example, in *Wolf Creek Collieries v. Sammons*, 142 F. App'x 854, 855-56 (6th Cir. 2005), the Sixth Circuit noted that even though Mrs. Sammons's case had already been in litigation for 29 years, the coal company was "certainly free to continue this Thirty Years War" using its § 922 modification right.

Coal miners and their survivors must endure years of litigation to get the modest black lung benefits to which they are entitled. The backlog before the Department of Labor's Office of Administrative Law Judges is the largest source of this delay.

III. If ALJs are found to be "officers of the United States," retroactive application of this decision will worsen the existing backlog of black lung cases.

A decision that opens the door for vacating or modifying past ALJ decisions due to the Appointments Clause will further burden an already overburdened system. Since 2009, the combination of a burgeoning caseload and dwindling staffing capacity has strained OALJ's ability to hear black lung benefits claims in a

timely way.[14] As a result, between 2009 and 2013 alone, OALJ's overall case backlog increased by 134%.

The consequence has been that ALJs received far more black lung claims than they are able to decide. In 2013, ALJs issued only 813 decisions despite the filing of 1,104 new black lung benefits claims and an additional 2,851 pending[15] cases at the ALJ level. By 2014, the number of pending cases increased to 3,142.[16] Black lung claimants were forced to wait an average of 429 days for their cases just to be assigned to an ALJ, and an additional 90 to 120 days for their cases to be heard.[17] On average, ALJs took 693 days, or nearly two years, to decide a black lung case.[18]

The backlog of black lung benefits claims before ALJs endures to this day despite increased funding from Congress[19] and an agency plan to reduce the backlog.[20]

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[14] *2015 OIG Report* at 5.

[15] A pending case is defined as a case that remains undecided more than one year after its filing.

[16] *Id.* at 4.

[17] *Id.* at 37.

[18] *Id.* at 12.

[19] Dep't of Labor, Fiscal Year 2019 Congressional Budget Justification, Departmental Management (2018), 5-6, *available at* https://www.dol.gov/sites/default/files/budget/2019/CBJ-2019-V3-02.pdf [hereinafter ***FY 2019 Budget***].

[20] *2017 OIG Report* at 9.

The most recent information from the Department of Labor projects that this backlog will, in fact, increase from 2,552 cases in FY 2017 to 2,724 black lung cases in FY 2018, before declining to 2,654 cases at the end of FY 2019. OALJ expects that, by 2019, it will still take an average of 20 months for ALJs to issue decisions in black lung cases.[21]

A decision here that applies retroactively could open the door to vacating and modifying past ALJ decisions in black lung cases. This, in turn, would exacerbate a backlog that already has serious human consequences. Many coal miners die before their black lung benefits claim is finally decided. The Federal Administrative Law Judges Conference agrees, arguing that "this decision will impact the more than 1930 current ALJs who are estimated to have well over one million pending cases. A lengthy or complicated process to review or rehear those cases could result in significant delays and increased backlogs."[22]

The most vulnerable black lung cases are those on direct appeal, where benefits were awarded prior to the Secretary of Labor's ratification of the ALJs' appointments. The most recent data shows that the Benefits Review Board has 441 pending black lung cases[23] and approximately 30 are before the U.S. Courts of Appeals. Even if only those nonfinal cases were affected, this

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[21] *FY 2019 Budget* at 54, 58.

[22] Brief Amicus Curiae of Federal Administrative Law Judges Conference in Support of Neither Party 12.

[23] *FY 2019 Budget* at 56.

would increase the OALJ backlog by 18% (from 2,724 to 3,195) – erasing any potential progress on the backlog and further delaying decisions for deserving coal miners and their survivors.

And while the awards on direct appeal are the most likely to be affected, because coal operators have the right to request modification under 33 U.S.C. § 922 of any award within a year that the last benefits were paid, *all* black lung beneficiaries who were awarded by ALJs prior to December 2017 become vulnerable.

The human toll of increased delays and case backlogs would be significant. In the words of Senator Bob Casey, "Justice delayed, as we often have said, is justice denied. In this case for coal miners suffering from the debilitating effects of black lung disease. Our nation's hard-working miners and their families deserve much better than that."[24]

IV. If a technical violation of the Appointments Clause exists, the Court should not apply its decision retroactively because doing so would cause injustice and hardship to individuals who have relied on ALJ decisions.

Even if a technical violation occurred in the appointment of ALJs, the Court should only apply its

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[24] *Coal Miners' Struggle for Justice: How Unethical Legal and Medical Practices Stack the Deck Against Black Lung Claimants: Hearing Before the Subcomm. on Employ't and Workplace Safety of the Senate Comm. on Health, Educ., Labor & Pensions*, 113th Cong. 5 (2014) (Prepared Statement of Senator Casey).

decision prospectively because a retroactive application severely harms individuals who have relied on ALJ decisions and would impose substantial inequitable results in individual cases.

Constitutional remedies are generally limited to the minimal remedy necessary to cure the constitutional defect. *See Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 508-09 (2010). In past Appointments Clause cases, the Supreme Court has refused to invalidate prior acts by improperly appointed officers. *See Buckley v. Valeo*, 424 U.S. 1, 142 (1976). Whether a decision should apply prospectively in civil cases has traditionally been governed by the nonretroactivity test articulated in *Chevron Oil Co. v. Huson*, 404 U.S. 97, 106-97 (1971). *See, e.g., Am. Trucking Ass'ns v. Smith*, 496 U.S. 167, 178 (1990). According to that test, the Court may apply a decision nonretroactively when the issue is of first impression and where the holding might be unfair or cause harm to individual parties if applied retroactively. *See Chevron Oil*, 404 U.S. at 106-07.[25]

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[25] The complete nonretroactivity test articulated by the Supreme Court in *Chevron Oil*:

> In our cases dealing with the nonretroactivity question, we have generally considered three separate factors. First, the decision to be applied nonretroactively must establish a new principle of law. . . . Second, it has been stressed that "we must . . . weigh the merits and demerits in each case by looking to the prior history of the rule in question, its purpose and effect, and whether retrospective operation will further or retard its operation." . . . Finally, we have weighed the inequity imposed

A. Historically, the Court has rejected retroactive application of its decisions when doing so would impair important government programs.

Considering the massive use of and reliance on ALJs across the federal government – including programs such as the black lung benefits program, Social Security, and immigration in which many individuals' livelihoods and safety depend – the interests in protecting both the functioning of government programs and the reliance interests of individuals are substantial. In the context of the black lung benefits program, a retroactive application of the law would severely impair the program because it would further burden already overburdened Department of Labor ALJ dockets. This harm to the program would substantially delay and interrupt access to benefits for thousands of former coal miners and their widows whose claims and livelihood rely on ALJ decisions. Rather, the Court should consider a prospective application of its holding as it has done in the past.

When the Supreme Court ruled in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 88 (1982), that the Bankruptcy Act intruded

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by retroactive application, for "(w)here a decision of this Court could produce substantial inequitable results if applied retroactively, there is ample basis in our cases for avoiding the 'injustice or hardship' by a holding of nonretroactivity."

404 U.S. at 106-07 (internal citations omitted).

upon Article III powers, the Court did not invalidate all decisions by bankruptcy judges who acted beyond their jurisdiction. Rather, the Court said that its decision would only apply prospectively because retroactive application in a case of first impression was not necessary to the holding and "would surely visit substantial injustice and hardship upon those litigants who relied upon the Act's vesting of jurisdiction in the bankruptcy courts." *Id.*

B. If the Court finds a constitutional violation, the Court should apply its decision nonretroactively or appropriately limit retroactive application to protect those who otherwise would be harmed.

Furthermore, even if a technical violation of the Appointments Clause in appointing Department of Labor ALJs occurred, the error was not prejudicial to any party. In December 2017, the Secretary of Labor ratified all Department ALJs. *See* U.S. Dep't of Labor, OALJ, *Home Page*, https://www.oalj.dol.gov/ (last visited Mar. 29, 2018) ("[T]he Secretary of Labor, R. Alexander Acosta, in his capacity as head of the Department of Labor, ratified the appointment of Chief Judge Stephen R. Henley on December 15, 2017 and of all other Department of Labor ALJs on December 21, 2017. The ratifications were effective immediately."). Congress clearly gave the Secretary of Labor authority to appoint ALJs for black lung claims. *See* 30 U.S.C. § 932a; *see also* 5 U.S.C. § 3105. Accordingly, any Appointments

Clause violations have been cured for Department of Labor ALJs.

Therefore, if the Court finds an Appointments Clause violation, retroactive application of that holding would be an empty formality within the Department of Labor, burdening all parties involved. The same ALJs who might have been improperly appointed have now been ratified. There is no reason to believe that voiding the old decisions and remanding for new ones would lead to different outcomes.

Instead of applying its decision purely retroactively, the Court should minimize harm to those receiving black lung benefits and others relying on ALJ decisions in one of two ways. First, the Court may hold that its decision regarding the appointment of ALJs will only be applied nonretroactively as in *Northern Pipeline*. Doing this would preserve the functioning of the black lung benefits program, among others, and in turn protect already vulnerable individuals from further harm.

Alternatively, retroactive application should be limited to cases where the Appointments Clause was properly raised and preserved – a very rare occurrence in the black lung context. In *Freytag v. Commissioner*, 501 U.S. 868, 878-80 (1991), the Court stated that the case was "one of those rare cases in which we exercise our discretion to hear petitioners' challenge" even though the petitioner waived it below. But it is notable that the Court ruled *against* the petitioner in *Freytag*. Justice Scalia's concurring opinion in *Freytag* on the importance of raising and preserving even Appointments

Clause challenges is instructive and was joined by three other justices. To find that such challenges cannot be waived has "no support in principle or in precedent or in policy." 501 U.S. at 895 (Scalia, J., concurring). Waiver of unraised issues is "not a mere technicality," it is "essential to the orderly administration of justice." *Id.* at 894-95 (quoting 9 C. Wright & A. Miller, Federal Practice and Procedure § 2472, p. 455 (1971)) (internal quotations omitted). For example, if the Court finds Appointments Clause challenges unwaivable, Department of Labor ALJs' prior decisions would be open to challenge, meaning that time spent on previous decisions will have been "expended uselessly." *Id.* at 900. The Court should make clear that where the losing party failed to properly and timely object, the challenge to an ALJ's appointment cannot succeed.

In addition, this case is about a Securities and Exchange Commission ALJ in the enforcement context. As the Court stated in *Free Enterprise Fund*, "many administrative law judges of course perform adjudicative rather than enforcement or policymaking functions." 561 U.S. at 507 n.10. Department of Labor ALJs perform purely adjudicative functions. For enforcement, a party must go to an actual officer: a U.S. District Judge. *See* 33 U.S.C. §§ 918, 921(d) (requiring a party to sue in U.S. District court to enforce an award of benefits); 20 C.F.R. § 725.351(c) (providing the "[p]owers of adjudication officer" and explaining that if a party disobeys an ALJ, the ALJ can only "certify the facts to the Federal district court having jurisdiction in the place in which he or she is sitting").

Even if the Court holds that the ALJ in this case was a constitutional officer, this does not mean that the Department of Labor's ALJs are "officers" when adjudicating black lung benefits claims. The Court should make clear that its decision should not affect past decisions from ALJs in other contexts such as the black lung benefits program.

CONCLUSION

The National Black Lung Association asks the Court to be mindful that if an Appointments Clause violation is found here that the Court's expression of its holding could affect coal miners and their families. The Court should seek to limit the impact of its decision on the black lung benefits program given (1) the increase in coal miners suffering from black lung, (2) the long delays and backlog before the U.S. Department of Labor's Office of Administrative Law Judges, and (3) the fact that Secretary Acosta has already ratified the appointment of all of the agency's ALJs. A holding otherwise would needlessly exacerbate the suffering caused by black lung. The Court should simply affirm the judgment below, but at minimum, the Court should limit

its holding to avoid disrupting the countless lives that depend on prior ALJ decisions.

Respectfully submitted,

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No. 17-130

In The Supreme Court of the United States

RAYMOND J. LUCIA AND
RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

BRIEF OF NATIONAL ORGANIZATION OF SOCIAL SECURITY CLAIMANTS' REPRESENTATIVES AS *AMICUS CURIAE* IN SUPPORT OF THE JUDGMENT BELOW

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INTEREST OF *AMICUS CURIAE*[1]

The National Organization of Social Security Claimants' Representatives (NOSSCR) is a nonprofit, voluntary membership association. NOSSCR has more than 2,900 members, mostly attorneys, who represent individuals seeking disability and other benefits under the Social Security Act. Individuals seeking such benefits have a right to request a hearing. *See* 42 U.S.C. § 405(b)(1). The Social Security Administration (SSA) employs more than 1,600 administrative law judges (ALJs) to preside over non-adversarial hearings to adjudicate individual claims for benefits.[2] SSA also uses ALJs to conduct adversarial hearings to enforce its rules of conduct and standards of responsibility for representatives. *See* 20 C.F.R. § 404.1765(b). NOSSCR members represent individuals at many of the hundreds of thousands of non-adversarial ALJ hearings held each year. While this case involves the question whether an ALJ employed by the Securities and Exchange Commission (SEC) is an "inferior Officer[ ]" for the purpose of the Appointments Clause, *see* U.S. Const. art. II, § 2, cl. 2, and thus directly affects the SEC's five ALJs,[3] the Court's answer to that question

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[1] Under Supreme Court Rule 37.6, NOSSCR states that no counsel for any party authored this brief in whole or in part; and that no person or entity, other than NOSSCR and its counsel, made a monetary contribution intended to fund the preparation and submission of this brief. All parties have filed blanket consents to the filing of *amicus curiae* briefs.

[2] Office of Personnel Mgt., *ALJs by Agency*, https://tinyurl.com/OPM-ALJs-By-Agency. All sites visited March 29, 2018.

[3] *ALJs by Agency*, *supra*.

may affect the much larger number of SSA ALJs as well as SSA's programs generally.

NOSSCR has two interests in this case. First, NOSSCR has an interest in SSA's ability to provide timely non-adversarial hearings for individuals seeking Social Security benefits. If this Court's decision spawns litigation over whether SSA ALJs are inferior Officers, then the adjudication of more than a million Social Security benefit claims may be delayed regardless of the outcome of such litigation. Second, NOSSCR has an interest in SSA ALJs providing full and fair non-adversarial hearings to individuals seeking Social Security benefits and, thus, an interest in the continuing decisional independence of SSA ALJs. If SSA ALJs are inferior Officers, then their decisional independence may be diminished.

INTRODUCTION

The Court granted certiorari on the question of whether an *SEC* ALJ is an Officer of the United States within the meaning of the Appointments Clause. *See* U.S. Const. art. II, § 2, cl. 2; *Freytag v. Comm'r of Internal Revenue*, 501 U.S. 868 (1991). As of March 2017, there were five SEC ALJs but more than 1,600 SSA ALJs.[4] Since an SEC ALJ and an SSA ALJ are both ALJs, the Court's decision will likely inform if not control the analysis whether an SSA ALJ is an inferior

[4] *ALJs by Agency*, *supra*.

Officer within the meaning of the Appointments Clause.

Since 1940, an individual seeking Social Security benefits has had a right to request a "hearing" to challenge SSA's denial of those benefits. *See* Social Security Act Amendments of 1939, 53 Stat. 1360; *see also* 42 U.S.C. § 405(b)(1). Since 1972, the adjudicator presiding over a hearing for Social Security benefits has been called an "administrative law judge." *See* 37 Fed. Reg. 16,787 (Aug. 19, 1972); *see also* Pub. L. No. 95-251, 92 Stat. 183 (1978) (renaming "hearing examiners" "administrative law judges"); 20 C.F.R. § 404.929 ("If you are dissatisfied with one of the determinations or decisions listed in [20 C.F.R.] § 404.930, you may request a hearing. The Deputy Commissioner for Disability Adjudication and Review, or his or her delegate, will appoint an [ALJ] to conduct the hearing."). SSA is the nation's largest adjudicative agency.[5] Its ALJs have conducted millions of non-adversarial hearings over the past three-quarters of a century.[6] In Fiscal Year 2016 alone, SSA ALJs disposed of more than 650,000 hearing requests, including after in-person or

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[5] *Cf. Heckler v. Campbell*, 461 U.S. 458, 461 n.2 (1983) ("The Social Security hearing system is 'probably the largest adjudicative agency in the western world.' ") (*quoting* J. Mashaw, C. Goetz, F. Goodman, W. Schwartz, P. Verkuil, & M. Carrow, *Social Security Hearings and Appeals: A Study of the Social Security Administration Hearing System* xi (1978)).

[6] *See* 20 C.F.R. § 404.900(b) ("In making a . . . decision in your case, we conduct the administrative review process in an informal, non-adversarial manner.").

video-conference hearings.[7] At the end of Fiscal Year 2017, more than one million hearing requests were pending before SSA ALJs.[8]

To NOSSCR's knowledge, the Commissioner of Social Security, acting as the Head of a Department, has not appointed SSA ALJs as inferior Officers.[9] *See* U.S. Const. art. II, § 2, cl. 2. NOSSCR is unaware of any public database specifying who appointed each of SSA's more than 1,600 ALJs. Since 1940, SSA's hearing examiners and (later) ALJs have decided millions of claims for Social Security benefits without controversy even though the hearing examiners and ALJs were not appointed as inferior Officers. Since 1940, stakeholders have assumed that SSA hearing examiners and ALJs did not need to be inferior Officers to decide individual claims for Social Security benefits after conducting non-adversarial hearings. Consistent with that assumption, NOSSCR is unaware of any precedent holding that an SSA ALJ who presides over a

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[7] Office of Retirement Policy, Soc. Sec. Admin., *Annual Statistical Supplement* (2017), tbl.2.F.9, https://tinyurl.com/SSA-Statistical-Supp-2017.

[8] Soc. Sec. Admin., *Agency Financial Report: Fiscal Year 2017* (Nov. 2017) (*Agency Financial Report*), 121, https://tinyurl.com/SSA-Financial-Report-FY2017.

[9] There is currently neither a Commissioner of Social Security nor an Acting Commissioner of Social Security to act as the Head of a Department to appoint SSA ALJs as inferior Officers. *See* U.S. Const. art. II, § 2, cl. 2. Nancy A. Berryhill, Deputy Commissioner for Operations, is performing the duties and functions not reserved for the Commissioner of Social Security. *See* Soc. Sec. Admin., *Nancy A. Berryhill*, https://www.ssa.gov/agency/commissioner.html.

non-adversarial hearing concerning an individual's claim for Social Security benefits is an inferior Officer with the meaning of the Appointments Clause.

If the Court holds that an SEC ALJ is not an inferior Officer, then almost certainly an SSA ALJ is likewise not an inferior Officer. However, if the Court concludes that an SEC ALJ is an inferior Officer, the Court should be cognizant of the looming question whether an SSA ALJ is also an inferior Officer. *See Bandimere v. SEC*, 844 F.3d 1168, 1190 (10th Cir. 2016), *petition for cert. pending*, No. 17-475 (filed Sept. 29, 2017) (commenting on possible consequences if an SSA ALJ is an inferior Officer); *id.* at 1200 (McKay, J., dissenting) (suggesting that an SSA ALJ is similar to an SEC ALJ). In articulating a rationale for any holding that an SEC ALJ is an inferior Officer, the Court should clearly distinguish between an SEC ALJ and an SSA ALJ, noting that the former, but not the latter, presides over an adversarial hearing and that whether a hearing is adversarial is relevant to determining whether the adjudicator is an inferior Officer for the purpose of the Appointments Clause. The Court should also take into account that well over one million pending and non-final claims for Social Security benefits would likely be affected if SSA ALJs are later found to be inferior Officers. At the end of Fiscal Year 2017, more than one million requests for hearing were pending before ALJs, and more than 94,000 requests for review of ALJ decisions were pending at SSA's Appeals

Council.[10] In Fiscal Year 2017, more than 18,000 civil actions were filed challenging SSA's final administrative decisions.[11] This case thus has the potential to disrupt SSA's programs and, consequently, to delay the payment of Social Security benefits to which individuals are entitled.

Finally, the Court should consider whether the decisional independence of SSA ALJs would be diminished if they were inferior Officers. For about the last decade, there has been a significant decline in the rate at which SSA ALJs decide that individuals are entitled to Social Security benefits.[12] There has been effective pressure on SSA ALJs to deny individuals Social Security benefits to which they are entitled, notwithstanding the existing civil service protections for SSA ALJs.[13] If SSA ALJs are inferior Officers, they may be under even greater political pressure to deny

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[10] *Agency Financial Report*, *supra*, 121. According to SSA's Inspector General, "The hearings and appeals process has experienced worsening timeliness and growing backlogs." *Id.*

[11] Soc. Sec. Admin., *Appeals to Court as a Percentage of Appealable AC Dispositions*, https://tinyurl.com/SSA-Appeals-Data.

[12] Government Accountability Office, *Social Security Disability: Additional Measures and Evaluation Needed to Enhance Accuracy and Consistency of Hearing Decisions* (Dec. 2017), 15, https://www.gao.gov/assets/690/688824.pdf.

[13] *See, e.g.*, Chris Joyner, "Judges pressured to deny disability appeals, one judge tells the AJC," *The Atlanta Journal Constitution* (Dec. 21, 2017) (reporting that Marilyn Zahm, President of the Ass'n of Admin. Law Judges, stated that "there is definite pressure from the agency to get judges to find against workers"), https://tinyurl.com/AJC-2017-Dec-21-Quote.

individuals the Social Security benefits to which they are entitled.

SUMMARY OF THE ARGUMENT

The Court should affirm the judgment below. Petitioners and Respondent demand a sea change in the constitutional status of ALJs within the SEC and, by necessary implication, in many other federal agencies. Both Petitioners and Respondent rely in part on the Administrative Procedure Act to support their view. *See* Pub. L. No. 79-404, 60 Stat. 237 (1946) (*codified at* 5 U.S.C. §§ 551-559). But that reliance is incongruent with the decades of ALJ adjudications pursuant to and consistent with the Administrative Procedure Act. The Administrative Procedure Act does not itself answer the question presented; the answer did not lie undiscovered in that statute for decades.

In addition, the Court below was correct in emphasizing that an SEC ALJ is not an inferior Officer because the ALJ's decision does not become final until the Commission issues an order.

ARGUMENT

I. The Administrative Procedure Act Itself Does Not Answer the Question Presented; the Administrative Procedure Act Applies to Both Adversarial and Non-Adversarial Adjudications

In *Freytag*, this Court held that special trial judges (STJs) of the Tax Court are inferior Officers for the purpose of the Appointments Clause based on three characteristics. 501 U.S. at 881-82. The office of STJ is established by law; the duties, salary, and means of appointment for that office are specified by statute; and STJs "exercise significant discretion" in "carrying out . . . important functions." *Id.* The question presented is whether SEC ALJs are inferior Officers of the United States within the meaning of the Appointments Clause. Petitioners and Respondent rely in part on the Administrative Procedure Act as a statute establishing ALJs by law and as authority that SEC ALJs in particular exercise significant discretion in carrying out important functions. Brief for Petitioners at 3, 12, 35-38, *Lucia v. SEC*, No. 17-130 (Feb. 21, 2018) (Pet'rs Br.); Brief for Respondent Supporting Petitioners at 11, 25, 29, *Lucia v. SEC*, No. 17-130 (Feb. 21, 2018) (Resp't Br.). The Administrative Procedure Act by itself does not answer the question presented.

Petitioners and Respondent correctly state that SEC ALJs conduct adversarial hearings. Pet'rs Br. at 2 ("Administrative law judges of the [SEC] preside over trial-like adversarial hearings"); Resp't Br. at 14 ("The Commission's ALJs, who preside over complex

adversarial disputes and issue initial decisions that often become the final decisions of the agency, wield significant authority on behalf of the United States. They are thus 'inferior Officers' who must be appointed in conformance with the Appointments Clause."). However, Petitioners and Respondent incorrectly assume or imply that any ALJ who conducts a hearing pursuant to or consistent with the Administrative Procedure Act conducts an *adversarial* hearing. The Administrative Procedure Act does not require an adversarial hearing. *See Richardson v. Perales*, 402 U.S. 389, 409 (1971).

An ALJ hearing under 42 U.S.C. § 405(b)(1) to determine whether an individual is entitled to Social Security benefits is non-adversarial. *See* 20 C.F.R. § 404.900(b) ("we conduct the administrative review process in an informal, non-adversarial manner"). In *Sims v. Apfel*, 530 U.S. 103 (2000), this Court recognized that proceedings before an SSA ALJ are "inquisitorial rather than adversarial. It is the ALJ's duty to investigate the facts and develop the arguments both for and against granting benefits." *Id.* at 110-11 (2000); *see also id.* at 111 (*citing* 20 C.F.R. § 404.900(b)). Likewise, in *Perales*, the Court stated that SSA's predecessor agency "operates essentially, and is intended so to do, as an adjudicator and not as an advocate or adversary." *Perales*, 402 U.S. at 403; *see also id.* 410 ("The social security hearing examiner, furthermore, does not act as counsel. He acts as an examiner charged with developing the facts."); 20 C.F.R. § 404.944 (SSA ALJ's regulatory duty to develop an adequate record); 20 C.F.R. § 404.1512(b)(1)-(2)

(describing SSA's responsibility to develop the medical record); 20 C.F.R. § 404.1512(b)(3) (describing SSA's responsibility to obtain vocational evidence).[14]

Consistent with the non-adversarial nature of an ALJ hearing under 42 U.S.C. § 405(b)(1) to adjudicate whether an individual is entitled to Social Security benefits, the Commissioner of Social Security is not represented by an attorney or a non-attorney at such a hearing. *See Sims*, 530 U.S. at 111. Because the Commissioner of Social Security is not represented by an attorney at a hearing under 42 U.S.C. § 405(b)(1), such a hearing is not an "adversary adjudication" for the purpose of the Equal Access to Justice Act (EAJA). *See* 5 U.S.C. § 504(a)(1) ("An agency that conducts an adversary adjudication shall award, to a prevailing party other than the United States, fees and other expenses incurred by that party in connection with that proceeding, unless the adjudicative officer of the agency finds that the position of the agency was substantially justified or that special circumstances make an award unjust."); 5 U.S.C. § 504(b)(1)(C) (defining "adversary adjudication" in part as "an adjudication under section

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[14] The SSA has extensive subregulatory guidance requiring its adjudicators, including ALJs, to develop the record with respect to specific issues. *E.g.*, Soc. Sec. Ruling 82-62 ("The decision as to whether the claimant retains the functional capacity to perform past work which has current relevance has far-reaching implications and must be developed and explained fully in the disability decision. Since this is an important and, in some instances, a controlling issue, every effort must be made to secure evidence that resolves the issue as clearly and explicitly as circumstances permit."). Social Security Rulings are binding on SSA adjudicators, including ALJs. *See* 20 C.F.R. § 402.35(b).

554 of this title in which the position of the United States is represented by counsel or otherwise"); *Sullivan v. Hudson*, 490 U.S. 877, 891 (1989) ("We agree with the Secretary that for purposes of the EAJA Social Security benefit proceedings are not 'adversarial' within the meaning of [5 U.S.C.] § 504(b)(1)(C)") (*citing Perales*, 402 U.S. at 403). The SEC ALJ who sanctioned Petitioners presided over an "adversary adjudication" for the purpose of 5 U.S.C. § 504.

In *Perales*, this Court did "not decide whether the APA has general application to social security disability claims, for the social security administrative procedure does not vary from that prescribed by the APA. Indeed, the latter is modeled upon the Social Security Act." 402 U.S. at 409.[15] Because the Court recognized that hearings for Social Security benefits under 42 U.S.C. § 405(b)(1) are consistent with the Administrative Procedure Act *and* non-adversarial, the Court recognized that the Administrative Procedure Act itself does not require an adversarial adjudication. In answering the question presented in *Lucia*, the Court should adhere to its analysis in *Perales* that an adjudication pursuant to or consistent with the Administrative Procedure Act may be adversarial *or* non-adversarial. Whether an ALJ "exercises significant discretion" in "carrying out . . . important functions" for the purpose of *Freytag* should depend in part on

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[15] *Cf. Mullen v. Bowen*, 800 F.2d 535, 536 n.1 (6th Cir. 1986) (en banc) ("Hearings under section 205(b), 42 U.S.C. § 405(b), must also conform to the Administrative Procedure Act, 5 U.S.C. §§ 556-557.").

whether the ALJ carries out those functions as part of an adversarial or a non-adversarial adjudication. Even if an SEC ALJ is an inferior Officer, an SSA ALJ who presides over a non-adversarial hearing concerning an individual's claim for Social Security benefits is not an inferior Officer but merely an agent of a principal. *Cf.* Brief for Court-Appointed *Amicus Curiae* in Support of the Judgment Below at 32-43, *Lucia v. SEC*, No. 17-130 (Mar. 26, 2018).

Because both SEC ALJs and SSA ALJs preside over administrative proceedings consistent with the Administrative Procedure Act, they not unexpectedly perform many of the same duties for their respective agencies. *See Bandimere*, 844 F.3d at 1200 (McKay, J., dissenting) ("SSA ALJs have largely the same duties as SEC ALJs"). Administrative law judges in both agencies perform basic adjudicative duties such as taking testimony from witnesses under oath, *see* 17 C.F.R. §§ 200.14(a)(1), (4), 201.325; 20 C.F.R. § 404.950(e); making evidentiary rulings, *see* 17 C.F.R. §§ 200.14(a)(3), 201.230; 20 C.F.R. §§ 404.935, 404.944, 404.950(c); and issuing subpoenas and denying requests for subpoenas, *see* 17 C.F.R. § 200.14(a)(2); 20 C.F.R. § 404.950(d).

Of necessity, ALJs in both agencies must *apply* the law to render decisions. But ALJs in both agencies do not have similar responsibilities to *interpret* the law. Whether an ALJ is an inferior Officer should depend, in part, on whether the ALJ has any policy-making role. The five SEC ALJs may *interpret* the law as a routine function. *See* Resp't Br. at 11 (SEC "ALJs issue

initial decisions that *interpret* and apply the law") (emphasis added). The more than 1,600 SSA ALJs have little, if any, occasion to *interpret* the law. The SSA requires its ALJs to apply the same law, including detailed subregulatory guidance, that its non-attorney adjudicators apply:

> We require adjudicators at all levels of administrative review to follow agency policy, as set out in the Commissioner's regulations, SSRs, Social Security Acquiescence Rulings (ARs), and other instructions, such as the Program Operations Manual System (POMS), Emergency Messages, and the Hearings, Appeals and Litigation Law manual (HALLEX). Under sections 205(a) and (b) and 1631(c) and (d) of the Act, the Commissioner has the power and authority to make rules and regulations and to establish procedures, not inconsistent with the Act, which are necessary or appropriate to carry out the provisions of the Act. The Commissioner also has the power and authority to make findings of fact and decisions as to the rights of any individual applying for payment under the Act. Because of the Commissioner's delegated authority to implement the provisions of the Act, we may, from time to time, issue instructions that explain the agency's policies, regulations, rules, or procedures. *All adjudicators must follow our instructions.*

Soc. Sec. Ruling 13-2p (emphasis added) (published at 78 Fed. Reg. 11,939, 11,946 (Feb. 20, 2013)).

II. Initial Decisions of SEC ALJs Become Administratively Final Only After the Commission Takes Action; Likewise, Some Decisions of SSA ALJs Become Administratively Final Only After SSA's Appeals Council Takes Action

The court below held that an SEC ALJ, who presides over an adversarial proceeding, is not an inferior Officer because the ALJ does not exercise "significant authority pursuant to the law of the United States" under *Buckley v. Valeo*, 424 U.S. 1 (1976). *See Raymond J. Lucia Cos., Inc. v. SEC*, 832 F.3d 277, 283-84 (D.C. Cir. 2016) (*citing Landry v. FDIC*, 204 F.3d 1125, 1133-34 (D.C. Cir. 2000)). For that holding, the court below emphasized that an SEC ALJ's initial decision is subject to discretionary review by the Commission and that an SEC ALJ's initial decision "becomes final when, and only when, the Commission issues the finality order, and not before." *Lucia*, 832 F.3d at 286 (*citing, e.g.*, 17 C.F.R. § 201.360(d)). "[T]he Commission has retained full decision-making powers, and the mere passage of time is not enough to establish finality." *Id.* The regulations governing the finality of an SSA ALJ's decision are similar, in part, to the regulations governing the finality of an SEC ALJ's initial decision.

The Social Security Act left it for the agency to determine if and when an SSA ALJ's decision becomes administratively final. *See Weinberger v. Salfi*, 422 U.S. 749, 766 (1975). The Appeals Council is SSA's highest

adjudicative body.[16] Some SSA ALJ decisions do not become administratively final until the Appeals Council takes action. An SSA ALJ may issue a "decision" or a "recommended decision." *See* 20 C.F.R. § 404.953(c) ("Although an [ALJ] will usually make a decision, the [ALJ] may send the case to the Appeals Council with a recommended decision based on a preponderance of the evidence when appropriate."). When an SSA ALJ issues a "recommended decision" that decision is not final until the Appeals Council issues its own "decision." *See* 20 C.F.R. § 404.979; *Hearings, Appeals and Litigation Law Manual* (*HALLEX*), § I-2-8-15(A). Thus, when an SSA ALJ issues a "recommended decision," that decision is similar in terms of administratively finality to an SEC ALJ's initial decision. An SEC ALJ's initial decision and an SSA ALJ's "recommended decision" are not final until the highest adjudicative body in the respective agency takes action.[17]

In the SEC's regulatory scheme, a party or aggrieved person has a right to file a petition for review of an ALJ's initial decision. 17 C.F.R. § 201.360(d)(1). A timely petition for review of an initial decision renders that decision non-final. 17 C.F.R. § 201.360(d)(1). In the SSA's regulatory scheme, an individual has a

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[16] *See* Soc. Sec. Admin., *Brief History and Current Information about the Appeals Council*, https://www.ssa.gov/appeals/about_ac.html.

[17] After receiving a "recommended decision," the Appeals Council need not issue its own "decision," but may instead remand a claim to an ALJ for further proceedings. *See HALLEX*, § I-2-8-15(A). A claim for Social Security benefits is not administratively final when it is remanded to an SSA ALJ for readjudication.

similar right, namely, a right to request Appeals Council review of an ALJ's decision. 20 C.F.R. §§ 404.967, 404.968; *see also Sims*, 530 U.S. at 106-07 (summarizing part of SSA's regulatory scheme). A timely request for Appeals Council review of an SSA ALJ's "decision" renders that decision non-final. *See* 20 C.F.R. § 404.955. When an individual files a timely request for Appeals Council review of an SSA ALJ's "decision," that "decision" becomes SSA's final administrative decision only if and when the Appeals Council denies the individual's request for review. *See* 20 C.F.R. § 404.981.

The Commission has a discretionary right to review the initial decision of an SEC ALJ. *See* 15 U.S.C. § 78d-1(b); 17 C.F.R. §§ 201.360(d)(2), 201.411(c). The Appeals Council has essentially the same authority when an SSA ALJ issues a "decision," including after a court remand.[18] *See* 20 C.F.R. § 404.969(a) ("[Any time] within 60 days after the date of a decision or dismissal that is subject to review under this section, the Appeals Council may decide on its own motion to review the action that was taken in your case."); 20 C.F.R. § 404.984(c) ("Any time within 60 days after the date of the decision of the [ALJ] [in a court-remand case], the Appeals Council may decide to assume jurisdiction of your case even though no written exceptions have

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[18] There are different regulations governing the finality of an SSA ALJ's "decision" depending on whether the "decision" is rendered after a court remand. *See* 20 C.F.R. § 404.970 (Appeals Council review in non-court remand case); 20 C.F.R. § 404.984 (Appeals Council review in court remand case).

been filed."). If the Appeals Council reviews an SSA ALJ's "decision" on its own motion in a non-court-remand case or assumes jurisdiction in a court-remand case, the SSA ALJ's "decision" is not administratively final. Rather, a later "decision" by the Appeals Council is SSA's administratively final decision. *See* 20 C.F.R. §§ 404.979, 404.984(c). If the Appeals Council remands a case to an SSA ALJ for further administrative proceedings instead of rendering a "decision," the ALJ's "decision" is vacated and the Appeals Council's remand order is not a final agency action. *See* 20 C.F.R. § 404.977.

An SEC ALJ's initial decision does not become administratively final merely due to passage of time. *See Lucia*, 832 F.3d at 286 (*citing* 17 C.F.R. § 201.360(d)). However, in some instances, an SSA ALJ's "decision" may become administratively final merely due to the passage of time. If an individual disagrees with an SSA ALJ's "decision" in a non-court-remand case, the individual must request Appeals Council review within sixty days of receipt of the "decision" to exhaust his or her administrative remedies. *See* 20 C.F.R. §§ 404.967, 404.968. If the individual does not request Appeals Council review of the ALJ's "decision" and if the Appeals Council does not review the ALJ's "decision" on its own motion within sixty days of the date of the "decision," the ALJ's "decision" is final and binding on both the individual and SSA. *See* 20 C.F.R. § 404.955.

The passage of time may also render administratively final an SSA ALJ's "decision" rendered on court remand. An individual who disagrees with an SSA

ALJ's "decision" on court-remand is not required to file exceptions to that "decision" with the Appeals Council to exhaust his or her administrative remedies; filing exceptions to an SSA ALJ's court-remand "decision" is optional. *See* 20 C.F.R. § 404.984. If an individual does not file exceptions to an SSA ALJ's "decision" on court remand within thirty days of receipt of the "decision" and if the Appeals Council does not assume jurisdiction within sixty days of that "decision," the ALJ's "decision" is administratively final without any further agency action. *See* 20 C.F.R. § 404.984(d). The passage of time thus may render administratively final an SSA ALJ's decision.

CONCLUSION

The Court should affirm the judgment below. An SEC ALJ is not an inferior Officer within the meaning of the Appointments Clause. But if the Court reverses the judgment below, it should take care to fashion its decision narrowly to avoid unwarranted implications putting at risk the well-established largest adjudicatory system in the Western World handling literally millions of Social Security claims.

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April 2, 2018

No. 17-130

In The Supreme Court of the United States

RAYMOND J. LUCIA, ET AL.,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION

On Writ of Certiorari to the
United States Court of Appeals
for the District of Columbia Circuit

BRIEF OF THE NEW CIVIL LIBERTIES ALLIANCE AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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In the Supreme Court of the United States

No. 17-130

RAYMOND J. LUCIA, ET AL., PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF OF THE NEW CIVIL LIBERTIES ALLIANCE AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

INTEREST OF AMICUS[1]

The New Civil Liberties Alliance (NCLA) is a nonprofit, public-interest law firm founded to challenge multiple constitutional defects in the modern administrative state through original litigation, amicus curiae briefs, and other means. The "civil liberties" of the organization's name include rights at least as old as the U.S. Con-

1. All parties consented to the filing of this brief. No counsel for a party authored any part of this brief. And no one other than the amicus curiae, its members, or its counsel financed the preparation or submission of this brief.

stitution itself, such as jury trial, due process of law, and the right to be tried in front of an impartial and independent judge whenever the government brings cases against private parties. Yet these selfsame civil rights are also very contemporary—and in dire need of renewed vindication—precisely because the Securities and Exchange Commission (SEC) and other administrative agencies have trampled them for so long.

NCLA aims to defend civil liberties—primarily by asserting constitutional constraints on the administrative state. Although Americans still enjoy the shell of their Republic, there has developed within it a very different sort of government—a type, in fact, that the Constitution's design sought to prevent. This unconstitutional state within the Constitution's United States is the focus of NCLA's concern.

Administrative rulemaking shifts much lawmaking from elected legislators to unelected bureaucrats, thereby removing it from a diverse people, placing it into the hands of a relatively homogenous few, and depriving Americans the benefit of equal voting rights. While this Court once justified the administrative adjudication of private rights as "prompt, continuous, expert, and inexpensive,"[2] this is no longer an apt description. Rather, at the SEC and elsewhere, administrative adjudication is often slow (as when Commissioners conduct appellate review), parochial (as when ALJs are barred from considering constitutional objections), inexpert (as detailed in the Argument below), and, of course, financially bur-

2. *Crowell v. Benson*, 285 U.S. 22, 46 (1932).

densome. To top it off, such adjudication violates procedural rights guaranteed by the Constitution.

The structural costs are severe. By giving the enforcement agency a second path for enforcement, administrative adjudication transforms procedural rights from constitutional guarantees into mere options for the exertion of governmental power. Perhaps worst of all, judicial deference to administrative interpretation and fact-finding corrodes the very judicial processes charged with keeping the Constitution's structural safeguards intact. For all these reasons, administrative power is the single greatest threat to civil liberties in our time.

NCLA agrees with the petitioners and the Solicitor General that administrative-law judges (ALJs) are "officers of the United States" subject to the Constitution's appointment rules. This amicus brief, however, underscores a key point about the *lack* of independence that ALJs enjoy. As the brief amply demonstrates, upholding the double-layered appointment of SEC ALJs would not protect their independence—in large part because they have very little independence to begin with under the current appointment regime. Hence, the Court can safely disapprove the existing appointment system without worrying about undermining ALJ independence.

STATEMENT OF FACTS

A. SEC's Appointment Process for ALJs

The SEC's administrative-law judges are sometimes—but not always—selected from a list of eligible candidates produced by the Office of Personnel Management (OPM). Pet. App. 295a–297a. OPM assembles

its list of eligible candidates after administering a competitive examination to aspiring ALJs. *See* 5 C.F.R. § 930.201(d)–(e). The SEC's chief administrative-law judge, along with an interview committee, considers the top three candidates on OPM's list and recommends one of them to serve as an ALJ. *See* 5 U.S.C. §§ 3317, 3318; 5 C.F.R. §§ 332.402, 332.404. This recommendation is subject to final approval by the SEC's Office of Human Resources. Pet. App. 297a.

Although it is commonly assumed that all SEC ALJs are appointed through this OPM process, *see* Pet. Br. 4 ("SEC ALJs are selected by SEC staff from a list of three candidates provided by the Office of Personnel Management."), that is not always the case. Sometimes the SEC does not want to limit itself to the three names produced by OPM, and it is allowed to circumvent this OPM process by hiring individuals who already serve as ALJs in other agencies. *See* 5 C.F.R. § 7.1; 5 C.F.R. § 315.501; Recommendations and Statements of the Administrative Conference Regarding Administrative Practice and Procedure, 57 Fed. Reg. 61760, 61761 (December 29, 1992) ("[M]ost agencies in recent years have found ways to circumvent this [OPM] process somewhat, primarily by hiring laterally from other agency ALJ offices."); Paul H. Verkuil, et al., *Administrative Conference of the United States Recommendations and Reports*, 1992 ACUS 942 ("The most prevalent way of circumventing the [OPM] register, however, is through 'lateral hiring'—transfer of ALJs between agencies.... OPM has recognized that this could provide some 'gaming' of the system."); Draft Report, American Bar Asso-

ciation, *Administrative Law Judges Under the Federal Administrative Procedure Act* (February 13, 2001), available at http://bit.ly/2GO9Kan (last visited on February 28, 2018) ("Agencies often prefer to avoid hiring ALJs off [OPM's] register. Instead, they hire ALJs laterally from other agencies. Lateral transfers are allowed after an ALJ has served at least one year in the agency making the original hire."). This practice enables the SEC to search for the most favorable candidates from among the 1,700 ALJs employed by the Social Security Administration (SSA), along with the countless number of ALJs who work for other federal agencies, rather than limiting itself to the three names on OPM's list. Indeed, three of the five SEC administrative-law judges—Brenda Murray, Carol Foelak, and Cameron Elliot—served as ALJs at other federal agencies before beginning their SEC stints.

The Enforcement Division has refused to say whether ALJs Murray and Elliot were hired through the OPM process. In a recent case involving Timbervest LLC, the Commission ordered the Enforcement Division to file an affidavit "setting forth the manner in which ALJ Cameron Elliot and Chief ALJ Brenda Murray were hired, including the method of selection and appointment."[3] The Enforcement Division responded with a cryptic statement that "ALJ Elliot was not hired through a process involving the approval of the individual members of the

3. *See* https://www.sec.gov/litigation/opinions/2015/ia-4096.pdf (last visited on February 28, 2018).

Commission."[4] The Division also filed an unsworn "Notice of Filing" that described the OPM process and stated that "[i]t is the Division's understanding that the above process was employed as to ALJ Elliot."[5]

But it is clear that the SEC did not follow the OPM process when it hired Cameron Elliot. Mr. Elliot himself has admitted as much. *See* Notice, http://bit.ly/2CprDyj (last visited on February 28, 2018) ("[D]uring a hearing in another case . . . ALJ Elliot expressed his belief that, because he transferred to his current position from the Social Security Administration, he was hired pursuant to a different process from that described in the Division's Notice of Filing."). So the SEC has far more control over the hiring process for ALJs than is typically assumed.

B. SEC's Proceedings Against Mr. Lucia

Petitioner Raymond J. Lucia is an investment professional who for nearly 40 years has had an unblemished record in his chosen profession. Mr. Lucia held free seminars for prospective clients that touted a retirement-planning strategy called "Buckets of Money," which urged a diversified portfolio from which investors would first liquidate lower-risk investments, while allowing the riskier investments more time to grow. Pet. App. 23a, 34a, 119a–120a, 127a–129a, 233a.

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4. *See* Affidavit of Seidman, https://www.sec.gov/litigation/apdocuments/3-15519-event-139.pdf (last visited on February 28, 2018).
5. *Ibid.*

Mr. Lucia used a slideshow that compared the outcomes for hypothetical investors who followed his strategy with those who followed other approaches. Two of the 126 slides in his slideshow were described as "backtests," which used actual historical data for stock-market returns alongside hypothetical assumptions regarding inflation and rates of return on real-estate and non-stock investments. All of the slides showing examples—including the two "backtest" slides—contained prominent disclaimers such as "This is a hypothetical illustration and is not representative of an actual investment." Pet. App. 43a n.10, 45a n.14, 47a n.19.

Mr. Lucia's slideshow was reviewed prior to public distribution by broker-dealers registered with the Financial Industry Regulatory Authority, who approved the slides and raised no concerns. Pet. App. 84a. And in 2003, SEC staff reviewed a similar presentation of Mr. Lucia's without raising any concerns that it might mislead. *Ibid.* No securities were offered or sold at Mr. Lucia's presentations, and none of the nearly 50,000 investors who have attended the seminars has ever filed a complaint alleging that the slides were misleading. Pet. App. 39a n.2, 82a, 129a, 206a.

Nevertheless, in 2012, the SEC charged Mr. Lucia with violating the antifraud provisions of the Investment Advisor's Act and SEC rules. The SEC claimed that Mr. Lucia had broken the law by using the word "backtest" when describing returns that combined actual historical data for stock-market returns with hypothetical assumptions about inflation and returns on non-stock investments during that time period. Pet. App. 7a-8a, 66a. Alt-

hough the word "backtest" is undefined in the law and in SEC regulations, and it had never before been construed in any judicial or administrative proceeding, the SEC's Enforcement Division insisted that a "backtest" must rely *exclusively* on historical data—even when a presentation explicitly discloses that hypothetical assumptions are being used. C.A.D.C. en banc JA 30.

The SEC had the option of bringing its enforcement action in federal court before an impartial and independent Article III judge who enjoys life tenure and salary protection. Instead, the SEC eschewed the Article III process and sued Mr. Lucia in its own administrative forum, where respondents have no right to a jury, a sharply curtailed right to discovery, and where the Federal Rules of Evidence are inapplicable. *See* Jean Eagleshem, *CFTC Turns Toward Administrative Judges*, Wall St. J. (November 9, 2014), http://on.wsj.com/2oDxXIX ("'We are going to use administrative proceedings more often,' [SEC Enforcement Director Andrew] Ceresney said. That will include some complicated cases, such as insider trading, that were once almost invariably tried in federal court, according to officials."). The case was assigned to ALJ Cameron Elliot, who has overwhelmingly ruled in favor of the Enforcement Division throughout his tenure, *see infra*, at 17, and who (unsurprisingly) found for the Commission and against Mr. Lucia in this case.

Asymmetries abound in these administrative proceedings. The SEC can spend years in burdensome investigations, *see* 15 U.S.C. § 78u(a)(1), yet respondents are generally allowed "approximately four months" for

limited discovery with little or no depositions. *See* 17 C.F.R. §§ 201.360(a)(2)(ii); 201.233(a). ALJs have broad discretionary powers to admit or exclude evidence, and they make factual and legal determinations that can be accepted without review or question by the Commission. And if no timely petitions for review are filed, or if the Commission declines review, an ALJ's decision "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. § 78d-1(c); accord 5 U.S.C. § 557(b) (ALJ's "initial decision" automatically becomes final "without further proceedings" absent further review.).

ALJ Elliot conducted a nine-day hearing, presiding over witness testimony and cross-examination. The ALJ made an initial finding of fraudulent misrepresentation on one investment strategy, but did not make factual findings on the SEC's remaining claims. Pet. App. 117a. The Commissioners then remanded the case back to the ALJ for fact-finding on the three remaining claims, noting the "vital role that initial decisions play in the Commission's decisional process." Pet. App. 241a. The Commission explained that the ALJ's determinations on the remaining claims would have "considerable importance" because the Commission itself had not "observed the parties and the witnesses." Pet. App. 241a.

On remand, the ALJ issued a revised initial decision finding that Mr. Lucia had willfully and materially misled investors and ordering draconian sanctions. He revoked Mr. Lucia's registration as a securities advisor; permanently barred him from associating with investment advisors, brokers, or dealers (including his own son); and

ordered more than $300,000 in civil monetary penalties. Pet. App. 225a–233a, 235a.

In reaching this decision, ALJ Elliot specifically credited the testimony of two witnesses—one of whom had admitted in writing that he knowingly made false statements against Lucia in an arbitration claim brought before the Financial Industry Regulatory Authority, while the other was described by the ALJ as having "holes in his memory." Pet. App. 193a-194a. At the same time, the ALJ never heard the proffer of evidence from other witnesses favorable to Mr. Lucia, as those pro-Lucia witnesses were intimidated into withdrawing by late-night subpoenas issued by SEC's Enforcement Division demanding all of their financial records, in every format, from any source, over a five-year period. Pet. Br. 7.

There was no evidence and no finding that any investor suffered any loss from the backtest marketing materials. Pet. App. 101a. Instead, ALJ Elliot cited "the substantial financial success" that Mr. Lucia and his company had supposedly "enjoyed at their clients' expense." Pet. App. 231a.

The Commission affirmed the ALJ's decision, over dissent, after Mr. Lucia sought review. The dissenting Commissioners—in the only written dissent of 2015—accused the majority of "creat[ing] from whole cloth specific requirements for advertisements that include the word 'backtest.'" Pet. App. 111a. The D.C. Circuit denied Mr. Lucia's petition for review after concluding that the SEC's liability findings were supported by substantial

evidence, and that the sanctions imposed were not an abuse of discretion. Pet. App. 21a–36a.

SUMMARY OF ARGUMENT

The petitioners and the Solicitor General have capably explained why SEC administrative-law judges qualify as "officers of the United States," who must be appointed in accordance with the process described in Article II of the Constitution. *See* Pet. Br. at 11–42; Resp. Br. at 10–38. NCLA writes as amicus to explain that the ostensible rationale for departing from the Constitution's appointment process—a desire to produce "independent" administrative-law judges—is inapplicable in this case, as the SEC's appointment process has failed to secure independent adjudication in any meaningful sense of the word.

SEC ALJs face significant institutional pressures to conform to the Commission's enforcement policy preferences. Not only must SEC ALJs follow agency rules, interpretations, and policies, but they also lack subject-matter expertise when appointed. This lack of prior expertise makes SEC ALJs vulnerable to pro-agency bias of various kinds, which they may not even recognize given how the bias is baked into agency precedent.

Avoiding the Appointments Clause has produced neither independence nor expertise among ALJs—quite the contrary. Hearings in front of ALJs at the SEC nowadays are neither impartial nor particularly expert. There is no reason for this Court to fear that declaring administrative-law judges to be "officers of the United States" will undermine the independence (or expertise) of agency adjudication, because the SEC's administra-

tive-law judges are short of independence and expertise to begin with. More effective and constitutionally permissible paths are available to secure independent judges in SEC proceedings.

ARGUMENT

I. The Current Appointment Process Does Not Secure the Independence of Administrative-Law Judges

SEC administrative-law judges have no institutional independence from the Commission, and the convoluted process for appointing these judges therefore does not further the goal of independent adjudication. ALJs face institutional pressures to favor SEC positions in enforcement proceedings; they are forbidden to question the legality or propriety of SEC rules and interpretations of statutes; and they do not conduct their hearings in an impartial and independent manner.

A. SEC ALJs Operate Under Institutional Pressures to Conform to the SEC's Wishes

The double-layered method of appointing SEC administrative-law judges does not secure their independence. Once appointed, the ALJs know that their decisions are subject to SEC review—and that the SEC can review their decisions on its own initiative when the losing party declines to appeal. *See* 17 C.F.R. §§ 201.410, 201.411(c). The ALJs must comply with the wishes of their overseers or face near certain reversal.

The ALJs also know that their cases are brought by the SEC in its prosecutorial role. So the Commission

that *appears before* an ALJ as a litigant will also be *reviewing* the ALJ's decisions. In every case, the ALJs must rule upon claims and arguments brought by the same entity that can review and reject or ultimately adopt their decisions.

Finally, the ALJs know that the SEC almost always decides in its own favor. From October 2010 through March 2015, the SEC ruled in the agency's favor in 95% of appeals taken from ALJ decisions. *See* Gideon Mark, *SEC and CFTC Administrative Proceedings*, 19 U. Pa. J. Const. L. 45, 48 (2016); Jean Eaglesham, *SEC Wins with In-House Judges*, Wall St. J. (May 6, 2015), http://on.wsj.com/1AKOxEH.

Under these circumstances, the ALJs have reason to issue rulings that anticipate their superiors' prosecutorial desires. This is not to suggest that the ALJs are deliberately biased in favor of the SEC, only that they face strong institutional pressures to align their decisions with SEC preferences.

One might protest that inferior Article III judges also dislike being overruled, and that the availability of review does not diminish their independence. But SEC ALJs are in a different position. They issue only initial decisions. *See* 17 C.F.R. § 201.360(a)(2). And if their decisions do not satisfy the prosecuting party, their decisions will not become final, and the prosecuting party will substitute its own decisions. *See* 15 U.S.C. § 78d-1; 17 C.F.R. §§ 201.410, 201.411(c). SEC ALJs therefore cannot even expect to have their decisions become final, unless they reach the results desired by the prosecuting party.

ALJs face other incentives to conform to the SEC's wishes. Their dockets, their prospects of promotion, and their future employment are subject to SEC control, and the Commission can wield its powers in a manner that rewards agency-friendly judges. For example, pending oversight from the Merit Systems Protection Board, the SEC can remove, suspend, demote, or reduce the salaries of ALJs for "good cause." 5 U.S.C. § 7521. Although a charge of good cause cannot be "base[d] on reasons which constitute an improper interference with the ALJ's performance of his quasi-judicial functions," *Brennan v. Dep't of Health & Human Servs.*, 787 F.2d 1559, 1563 (Fed. Cir. 1986), this nonetheless leaves room to remove and otherwise penalize ALJs for conduct "inconsistent with maintaining confidence in the administrative adjudicatory process," *Long v. Soc. Sec. Admin.*, 635 F.3d 526, 536 (Fed. Cir. 2011), including "adjudicatory errors" over a range of cases. *Social Sec. Admin., Office of Hearings and Appeals v. Anyel*, M.S.P.B.1993, 58 M.S.P.R. 261, 268–69, opinion after remand 66 M.S.P.R. 328 (finding "good cause" in an ALJ's "adjudicatory errors" and in her "'[i]ndependence' consisting of freedom to ignore binding agency interpretations of law").

ALJs know that they can pay a price for deviating too much from the SEC's expectations, and at least one SEC ALJ has protested that she was admonished.[6] They can-

6. *See* Jean Eaglesham, *SEC Wins with In-House Judges*, Wall St. J. (May 6, 2015), http://on.wsj.com/1AKOxEH (reciting complaints of former ALJ Lillian McEwen), detailed in Part I.C below.

not help but be aware of the ALJ purge that occurred at the U.S. Commodity Futures Trading Commission ("CFTC"). That agency abandoned its long-held preference for administrative adjudication after an "almost decade-long losing streak before one of its own ALJs" prompted the change.[7] The CFTC thereafter eliminated two ALJs and their associated staff, and terminated one ALJ through a reduction-in-force (RIF) in 2012.[8] Reduction in force is an exception to the "good cause" requirement for removing ALJs, *see* 5 U.S.C. § 7521(b), meaning that an agency can simply clear its decks of unwanted ALJs. *See* Federalist, No. 79 (Hamilton) ("In the general course of human nature, a power over a man's subsistence amounts to a power over his will."). Conversely, compliant ALJs can be rewarded for their loyalty, as the SEC recently demonstrated in its November 30, 2017, order ratifying and reappointing its five agency-friendly ALJs.[9]

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7. Gideon Mark, *SEC and CFTC Administrative Proceedings*, 19 U. Pa. J. Const. L. 45, 60 (2016).

8. GAO Letter of January 23, 2013, available at https://www.gao.gov/assets/660/651588.pdf (last visited on February 28, 2018).

9. On November 30, 2017, the day after the Solicitor General submitted a brief in this case taking the position that the SEC's ALJ appointments were inconsistent with the Constitution's Appointments Clause, the SEC issued an official Press Release announcing that the Commission "has ratified its prior appointment of Chief Administrative Law Judge Brenda Murray, and Administrative Law Judges Carol Fox Foelak, Cameron Elliot, James E. Grimes and Jason S. Patil." *See* https://www.sec.gov/news/press-release/2017-215 (last visited on February 28, 2018). The press release further asserted: "By ratifying the appoint-

(continued...)

B. SEC ALJs Must Follow Agency Rules, Interpretations, and Other Policies

When the SEC litigates in an Article III forum, the court may—indeed, must—review the legality of the agency's rules, its interpretations of statutes, and its other policies and pronouncements. *See* 5 U.S.C. § 706 (instructing courts to "hold unlawful and set aside agency action, findings, and conclusions found to be" unlawful). As Chief Justice Marshall explained, "It is emphatically the province and duty of the judicial department to say what the law is. Those who apply the rule to particular cases, must of necessity expound and interpret that rule. If two laws conflict with each other, the courts must decide on the operation of each.... This is of the very essence of judicial duty." *Marbury v. Madison*, 5 U.S. 137, 177 (1803).

Not so in agency adjudication, where the SEC's administrative-law judges are forbidden to depart from or question the legality of the agency's rules—even if the defendant is challenging their validity. *See Arizona Grocery Co. v. Atchison*, 284 U.S. 370 (1932). Worse, the ALJs are also forbidden to consider challenges to the lawfulness or validity of the SEC's organic statutes. *See Milton J. Wallace*, Exchange Act Release No. 11252, 1975 SEC Lexis 2238, at *7 (February 14, 1975) (declar-

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ment of its ALJs, the Commission has resolved any concerns that administrative proceedings presided over by its ALJs violate the Appointments Clause. The Commission Order also directs the ALJs to review their actions in all open administrative proceedings to determine whether to ratify those actions." *Ibid.*

ing that the SEC (and thus an SEC ALJ) has "no power to invalidate the very statutes that Congress has directed [it] to enforce."). So the ALJs' hands are partially tied whenever they adjudicate an enforcement proceeding. And this gives the SEC a built-in advantage whenever it brings enforcement actions before its ALJs.

C. SEC ALJs Do Not Conduct Hearings in an Impartial and Independent Manner

The SEC contends that its ALJs "conduct public hearings in a manner similar to federal bench trials." SEC, Office of Administrative Law Judges (page last modified January 26, 2017), at https://www.sec.gov/alj. Much evidence casts doubt on this assertion.

To begin, the SEC's rate of success before its ALJs is considerably higher than its rate of success in federal court. From October 2010 to September 2015, the SEC "prevailed against 86% of respondents in contested cases heard by ALJs" but "had a considerably lower success rate of 70% in federal court." Gideon Mark, *SEC and CFTC Administrative Proceedings*, 19 U. Pa. J. Const. L. 45, 47 (2016). Indeed, the SEC ALJ who presided in Mr. Lucia's case has demonstrated an astonishing record of fealty to his agency. *See* Jean Eaglesham, *Fairness of SEC Judges Is in Spotlight*, Wall St. J. (November 22, 2015) ("Judge Cameron Elliot, a 49-year-old former nuclear-submarine officer and SEC judge since 2011, has found the defendants liable in every contested case he has heard, the analysis showed.... Mr. Elliot told the defendants during settlement discussions on a case they should be aware he had never ruled against the agency's enforcement division").

None of these data or anecdotes should be surprising. In a 1992 survey of ALJs, 15 percent complained of threats to their independence, while 9 percent reported that threats of this sort were a frequent problem. *See* Charles H. Koch Jr., *Administrative Presiding Officials Today*, 46 Admin. L. Rev. 271, 278 (1994). One of the SEC's former administrative-law judges has publicly complained that she had been pressured to reach decisions favorable to the Commission. *See* Jean Eaglesham, *SEC Wins with In-House Judges*, Wall St. J. (May 6, 2015), http://on.wsj.com/1AKOxEH ("Lillian McEwen, who was an SEC judge from 1995 to 2007, said she came under fire from Ms. Murray [the SEC's chief administrative-law judge] for finding too often in favor of defendants. 'She questioned my loyalty to the SEC,' Ms. McEwen said in an interview, adding that she retired as a result of the criticism."). Chief ALJ Murray remains on the job.

Finally, administrative-law judges can reverse the burdens of proof. When litigating enforcement actions in an Article III forum, the SEC must always bear the burden of proof on disputed questions of fact—and in criminal proceedings the SEC must prove its case beyond a reasonable doubt. *See In re Winship*, 397 U.S. 358, 364 (1970).

ALJs, however, can reverse such burdens by taking "official notice" of facts. 5 U.S.C. § 556(e). Unlike federal district-court judges, who are confined to the evidence introduced by the parties and face strict limits on taking

"judicial notice" of facts outside the record,[10] SEC ALJs can take notice of any material fact—regardless of whether it appears in the record, is adjudicative, falls within the expertise of the agency, or is subject to reasonable dispute. *See* SEC Rules of Practice, § 111, at https://www.sec.gov/about/rulesprac072003.htm#323 ("No provision of these Rules of Practice shall be construed to limit the powers of the hearing officer provided by the Administrative Procedure Act, 5 U.S.C. §§ 556, 557."). Worse, an ALJ can do all of this without a hearing, which is available to parties whenever a district-court judge takes judicial notice of facts. *See* Fed. R. Evid. 201(e) ("On timely request, a party is entitled to be heard on the propriety of taking judicial notice and the nature of the fact to be noticed. If the court takes judicial notice before notifying a party, the party, on request, is still entitled to be heard."). ALJs thus have a sweeping power to take notice even of disputed facts. To be sure, when an ALJ takes notice of facts, a defendant can ask the ALJ for "an opportunity to show the contrary." 5 U.S.C. § 556(e). But the effect is to shift the burden of proof to the defendant, who now must introduce evidence to *disprove* facts of which the ALJ has taken "official notice."[11]

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10. *See* Fed. R. Evid. 201(b) ("The court may judicially notice a fact that is not subject to reasonable dispute because it: (1) is generally known within the trial court's territorial jurisdiction; or (2) can be accurately and readily determined from sources whose accuracy cannot reasonably be questioned.").

11. Not merely when SEC ALJs take notice of facts, but throughout their proceedings, they are said to reverse the burden of

(continued...)

In one way after another, ALJs at the SEC lack the requisite impartiality and independence under the current appointment regime. Nothing will be lost by disapproving this mode of appointment.

II. Lack of Prior Background or Expertise in Securities Law Renders SEC ALJs Vulnerable to Agency Bias and Influence

A. SEC's ALJs Lack Prior Securities Law Expertise

Defenders of agency tribunals sometimes assert that administrative-law judges have (or develop) special expertise in the legal issues and subject matter of their agency—and that the benefits of this expertise outweigh the pathologies that arise from administrative adjudication. *See, e.g.*, Gideon Mark, *SEC and CFTC Administrative Proceedings*, 19 U. Pa. J. Const. L. 45, 117 (2016) (arguing that one of the "countervailing benefit[s] of administrative adjudication" before the SEC derives from its "agency ALJs who develop an expertise in the federal securities laws"). But the SEC's ALJs do not appear to have had *any* background in securities before their appointments, and the publicly available résumés of these individuals evince no previous experience in the field.

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proof. *See* Jean Eaglesham, *SEC Wins with In-House Judges*, Wall St. J. (May 6, 2015), http://on.wsj.com/1AKOxEH (quoting a former SEC administrative-law judge who alleged that "the burden was on the people who were accused to show that they didn't do what the agency said they did.").

The most recent SEC administrative-law judge, appointed in September 2014, worked in the U.S. Department of Justice from 1998 to 2012 as an attorney in the Executive Office for Immigration Review and as a trial attorney litigating civil cases, including litigation surrounding the anthrax letter attacks and involving the World Trade Center site post-9/11. He also spent time in Egypt and Iraq as a government attorney.[12]Another SEC ALJ, who was appointed in June 2014, previously spent 13 years in the U.S. Department of Justice as senior litigation counsel in the civil division and worked in the U.S. Navy's Judge Advocate General's Corps, first as a trial defense counsel for service members facing court-martial and later as an appellate counsel representing the government before military appellate courts.[13]

An ALJ appointed in April 2011 appears to have previous service as an ALJ for the Social Security Administration, some years of practice of intellectual-property law, service as an assistant U.S. Attorney in the Southern District of Florida and the Eastern District of New York, and work as a trial attorney in the U.S. Department of Justice, where he handled patent and copyright cases.[14]

The biographies for the two longest-tenured ALJs appointed in the 1990s do not appear anywhere on the

12. *See* https://www.sec.gov/news/press-release/2014-208 (last visited on February 28, 2018).

13. *See* https://www.sec.gov/news/press-release/2014-129 (last visited on February 28, 2018).

14. *See* https://www.sec.gov/news/press/2011/2011-96.htm (last visited on February 28, 2018).

SEC's website. Chief ALJ Brenda Murray's bio was published in conjunction with her appearance at a 2015 conference on "Women, Prison, and Gender-Based Violence," and (like those of her colleagues) it does not reveal any background or prior experience in securities law.[15] The final ALJ spent 29 years as a staffer at the Federal Communications Commission before becoming an ALJ at the Social Security Administration and then a short time later an ALJ at the SEC.

B. A Lack of Prior Expertise Makes It Harder for ALJs to Resist Sources of Pro-Agency Bias

ALJs who lack any background or experience in securities law before joining the agency will be more susceptible to SEC influence. A securities-law novice will be far more reluctant than a seasoned expert to second-guess or stand up to the Commission's enforcement efforts. Such trepidation further aggravates the independence problems that afflict SEC's in-house adjudication regime.

One source of potential bias derives from the blinders that ALJs are forced to wear. Unlike Article III judges, ALJs at the SEC (and elsewhere) are not allowed to question the constitutionality or legality of the laws or regulations they adjudicate. They must ignore any claims by a defendant that an authorizing statute violates the Constitution (whether on its face or as applied),

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15. *See* http://www.lawschool.cornell.edu/womenandjustice/Conferences-and-Events/upload/2015-Conference-Bios-FINAL-2.pdf (last visited on February 28, 2018).

and they may not pass judgment on whether a regulation is authorized by statute. By routinely ignoring claims of this sort, the ALJs can become desensitized to the agency's error rate, and can wind up viewing the agency as closer to infallible than it really is. This misperception is especially likely to occur when an ALJ's only experience with SEC cases comes while sitting as an ALJ. Because federal district-court judges are not similarly constrained in the arguments that they may consider, they do not risk having their perception skewed in this manner. The unquestioned allegiance that ALJs must display toward the SEC's statutory and regulatory regime no doubt contributes to the higher success rates that the Enforcement Division enjoys before its ALJs as compared to federal district-court judges.

A second source of bias arises from the ratchet effect of the Commission's appellate review. The Enforcement Division almost invariably appeals to the Commission when it loses before an ALJ. In contrast, defendants increasingly do not appeal adverse ALJ rulings, for reasons of expense and futility. Furthermore, when the Commission reviews an ALJ judgment, it is highly likely to adopt the Enforcement Division's position—after all, the Commissioners were the ones who approved the enforcement case and the underlying enforcement policies. So ALJ decisions in the Commission's favor are rarely overruled on appeal, while ALJ decisions in a defendant's favor are much more likely to be reversed by the Commission. Over time this means that outlier legal rulings in the defendant's favor are far more likely to be corrected than erroneous ones favoring the SEC. This

lopsided review mechanism leads to an undue accretion of pro-SEC rulings, which virtually ensures that the Commission's precedents will be stretched in the agency's favor. This biased body of SEC precedent also becomes part of the agency knowledge that new ALJs encounter when they first join the agency, and from which they acquire their expertise in securities law. When they do not bring their own prior subject-matter expertise with them, they are not well equipped to recognize or overcome the biased effect of the agency precedents.

Yet another source of bias arises from the fact that many ALJs—including the judge who presided in this case—are hired from the pool of Social Security Administration ALJs. *See* Draft Report, American Bar Association, *Administrative Law Judges Under the Federal Administrative Procedure Act* (February 13, 2001), available at http://bit.ly/2GO9Kan (last visited on February 28, 2018) ("Approximately 900 of the 1,200 ALJs hear benefits cases for the SSA. Therefore, most agencies prefer to hire from the abundance of experienced SSA ALJs, rather than hiring off a strict register. As a result, only the SSA significantly relies on the OPM selection process to hire their ALJs."). SSA judges determine eligibility for government benefits, and in this context, the burden of proof appropriately lies with the claimant, and the government's success rate is understandably high. In contrast, in SEC adjudications—where the government is charging defendants with violations of law and is threatening to deprive them of their livelihood, future employment, and reputation, and to impose severe financial penal-

ties—the burden of proof should be on the government. But ALJs accustomed to ruling for the government may not give defendants their due. Former SSA judges, in particular, are apt to adjudicate the binding constraints at stake in SEC cases as if they were akin to benefits at stake in SSA cases.[16] Where an ALJ lacks prior subject-matter expertise—and thus familiarity with binding constraints and rights-based defenses—there is a further danger of bias in the agency's favor.

There is reason to think that SEC is aware of the factors that could lead ALJs to favor the agency. As discussed above, the Commission has often skipped the OPM merit selection process in favor of plucking its ALJs directly from the pool of ALJs at other agencies. Why does it do this? And given that it thereby greatly expands the pool of candidates, why does it nonetheless select candidates who do not bring subject-matter expertise with them? There is at least the possibility that the SEC has learned that it is better able to identify ALJs who have a propensity for (or track record of) favoring the government when it uses this selection method.

Selecting ALJs directly from other agencies further undercuts the independence of all ALJs, because by now a majority of the ALJs at the SEC has been appointed in this way. When the Enforcement Division brings a case in front of these judges—none of whom has a securities-

16. This difference—between ALJs who adjudicate benefits and ALJs who adjudicate binding constraints—also forms the basis for a valid and workable distinction, under which the Appointments Clause applies in the SEC adjudication context, even if not necessarily in benefits-adjudication contexts.

defense background—it does not have to worry as it would in federal district court about drawing a judge who might embarrass the Commission by ridiculing a far-fetched legal theory or weak case propounded by the Enforcement Division. This fact alone affects the cases SEC is willing to bring, the legal interpretations it is prepared to advance, and the extent to which it will warp the law in pursuit of enforcement.

One can also imagine that ALJs plucked from relative obscurity at other agencies for a plum position at the SEC will feel especially beholden to the agency that hand-picked them—much more so than would an ALJ selected through the usual OPM selection process.

C. Avoiding the Appointments Clause Results in Less Expertise—Not More Independence—for ALJs

The myth that agency adjudication is conducted by experts appointed for their command of securities law does not withstand an examination of the facts. This Court should not balk at noticing that the expertise emperor has no clothes. Officers of the United States at SEC who were appointed pursuant to the Appointments Clause (*e.g.*, SEC Commissioners) have historically tended to bring relevant, pre-existing securities-law expertise with them to the agency. But when the Constitution's appointments process has been avoided, as with the appointment of ALJs at the SEC, those appointees have historically tended *not* to have relevant, pre-existing securities-law expertise. Hence, one can fairly conclude that ignoring the constitutional appointments process does not enhance the independence of ALJs; in-

stead, the trade-off is to reduce the relative expertise of such appointees (and the independence that subject-matter expertise brings) by deviating from the constitutional appointments process.

For these reasons this Court should not worry that disapproving the current ALJ appointment process will jeopardize the independence of ALJs at SEC. Far from it.

III. More Effective and Constitutionally Permissible Paths Exist to Securing Independent Judges in SEC Proceedings

Providing for independent judges in SEC enforcement proceedings is a worthy goal. But the current appointment process for ALJs does not further that end. So even if one thought that it were *possible* to interpret the Constitution in a manner that excludes ALJs as "officers of the United States"—and NCLA does not think this is possible, for the reasons provided by the petitioners and the Solicitor General—there is no *reason* to adopt this interpretation when the current regime fails to produce any semblance of independent adjudication.

The good news is that there is an effective (and constitutionally permissible) means of providing independent adjudicators—and it is hiding in plain sight in the language of the Constitution. Article III provides that the "judicial Power of the United States" shall be vested in the Supreme Court and in the "inferior courts" established by Congress, whose judges "shall hold their Offices during good Behaviour" and whose compensation "shall not be diminished during their Continuance in Of-

fice." U.S. Const. art. III. *This* is the mechanism that the Constitution provides for securing independent adjudicators in SEC enforcement proceedings.

Article III provides all that is needed to secure the independence of those who adjudicate SEC enforcement proceedings. Article III judges are principal officers chosen by the President and Senate together, rather than inferior officers selected by the SEC's Commissioners or mere "employees" selected by the SEC's chief ALJ. The decisions of Article III judges are never subject to review by the Commission, so they have no reason to conform their rulings to the SEC's wishes. And the Constitution gives Article III judges life tenure and protects their salaries from diminution, so Article III judges have no rational reason to fear ruling against the SEC.

Article III judges are also empowered to review the legality of SEC rules and statutory interpretations—unlike administrative-law judges, who are bound to follow SEC rules even if they believe them to be unlawful or unconstitutional. *See Arizona Grocery*, 284 U.S. 370. And as far as NCLA is aware, there have been no reports that contemporary Article III judges have ever felt pressured to rule in favor of administrative agencies. *Compare* Jean Eaglesham, *SEC Wins with In-House Judges*, Wall St. J. (May 6, 2015), http://on.wsj.com/1AKOxEH.

Article III judges enjoy added independence from their status as generalists. It is difficult, if not impossible, to pack the federal judiciary with either SEC or industry partisans, because the President and the Senate have many other priorities to consider when selecting

federal judges. In addition, political control of the Presidency and the Senate cycles over time between the two parties, which makes it even more difficult to consistently appoint Article III judges who show favor toward SEC enforcement efforts or the financial-services industry, or who hold any type of agenda with regard to the SEC.

Finally, the costs of replacing SEC ALJs with Article III judges are low. There are only five ALJs at the SEC, and the federal district courts can easily absorb a docket that is currently handled by five individuals. If there is to be truly independent adjudication in future SEC enforcement proceedings, then the solution is to move those proceedings to Article III courts, not to establish half-baked "independence" measures that flout the Constitution's appointment rules.

Meanwhile, this Court need not fear that any independence (or expertise) will be lost by disapproving the current SEC ALJ appointment regime. Hearings in front of ALJs at the SEC nowadays are neither impartial nor particularly expert.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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No. 17-130

In the
Supreme Court of the United States

RAYMOND J. LUCIA, et al.,
Petitioners,

v.

SECURITIES AND
EXCHANGE COMMISSION,
Respondent.

On Writ of Certiorari
to the United States Court of Appeals
for the District of Columbia Circuit

BRIEF AMICUS CURIAE OF PACIFIC LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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INTEREST OF AMICUS CURIAE[1]

Founded in 1973, Pacific Legal Foundation is a nonprofit, tax-exempt corporation organized under the laws of the State of California for the purpose of engaging in litigation in matters affecting the public interest. PLF provides a voice in the courts for mainstream Americans who believe in limited government, private property rights, individual freedom, and free enterprise.

PLF is the most experienced public interest legal organization defending the constitutional principle of separation of powers in the arena of administrative law. PLF's attorneys have participated as lead counsel or counsel for amici in several cases before this Court involving the role of the Article III courts as an independent check on the Executive and Legislative Branches under the Constitution's Separation of Powers. *See, e.g., Nat'l Ass'n of Mfrs. v. Dep't of Def.*, 138 S. Ct. 617 (2018); *Gloucester Cnty. Sch. Bd. v. G.G. ex rel. Grimm*, 136 S. Ct. 2442 (2016) (*Auer* deference to agency guidance letter); *U.S. Army Corps of Eng'rs v. Hawkes Co., Inc.*, 136 S. Ct. 1807 (2016) (judicial review of agency interpretation of Clean Water Act); *Sackett v. EPA*, 566 U.S. 120 (2012) (same); *Decker v. Nw. Envtl. Def. Ctr.*, 568 U.S. 597 (2013) (*Auer* deference to Clean Water Act regulations); *Rapanos v.*

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[1] Pursuant to this Court's Rule 37.3(a), all parties have consented to the filing of this brief. Letters evidencing such consent have been filed with the Clerk of the Court.

Pursuant to Rule 37.6, Amicus Curiae affirms that no counsel for any party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than Amicus Curiae, its members, or its counsel made a monetary contribution to its preparation or submission.

United States, 547 U.S. 715 (2006) (agency regulations defining "waters of the United States").

PLF supports the Petitioners in this case because it raises core Separation of Powers issues related to each co-equal branch's accountability for the exercise of its powers. PLF's policy perspectives and litigation experience offer an additional viewpoint that will assist the Court in reviewing this case.

INTRODUCTION AND SUMMARY OF ARGUMENT

This Court has consistently reaffirmed the central judgment of the Framers that the "ultimate purpose of th[e] separation of powers is to protect the liberty and security of the governed." *Metro. Wash. Airports Auth. v. Citizens for the Abatement of Aircraft Noise, Inc.*, 501 U.S. 252, 272 (1991). Indeed, "[n]o political truth is certainly of greater intrinsic value or is stamped with the authority of more enlightened patrons of liberty." *The Federalist No. 47*, at 324 (James Madison) (J. Cooke ed. 1961).

Therefore, the liberty and security of the governed are threatened when the carefully balanced scheme of the Framers is not enforced.

In particular here, the question of whether SEC administrative law judges are Officers of the United States within the meaning of the Appointments Clause implicates the important principle that government must be accountable to the governed. *See Edmond v. United States*, 520 U.S. 651, 660 (1997) ("By requiring the joint participation of the President and the Senate, the Appointments Clause was designed to ensure public accountability for both the making of a bad appointment and the rejection of a good one."); *Freytag v. Comm'r of Internal Revenue*,

501 U.S. 868, 878 (1991) ("The Appointments Clause not only guards against this encroachment [of one branch at the expense of the others] but also preserves another aspect of the Constitution's structural integrity by preventing the diffusion of the appointment power."); Elena Kagan, *Presidential Administration*, 114 Harv. L. Rev. 2245, 2332 (2001) ("The lines of responsibility should be stark and clear, so that the exercise of power can be comprehensible, transparent to the gaze of the citizen subject to it.") (internal quotation marks and citation omitted). *Cf. Dep't of Transp. v. Ass'n of Am. R.R.s*, 135 S. Ct. 1225, 1234 (2015) (Alito, J., concurring) ("Liberty requires accountability.").

The lines of responsibility become blurred, and accountability for the exercise of power becomes less comprehensible, when Congress authorizes executive-branch employees to exercise duties of an "Officer of the United States" without subjecting their appointments to the strictures of the Appointments Clause. The growth of the Administrative State—with its ever-increasing oversight by individuals wielding significant power—demands accountability.

The decision below, if allowed to stand, would reduce that accountability. Petitioners were subjected to an administrative enforcement action initiated by the Enforcement Division of the Securities and Exchange Commission and conducted by an SEC Administrative Law Judge. Pet. App. 37a-38a. In this proceeding, Administrative Law Judge Cameron Elliot heard testimony, including expert-witness testimony; ruled on the admissibility of evidence; considered and ruled on objections; weighed evidence; made factual findings; and reached legal conclusions.

Id. at 115a-237a (ALJ Initial Decision on Remand). Judge Elliot ruled that Petitioners had violated the Investors Advisers Act of 1940, and he issued sanctions: permanently barring Petitioner Raymond Lucia from working as an investment advisor, revoking his (former) company's registration, and imposing civil penalties in the amount of $300,000. *Id.* at 235a.

Petitioners argued that this administrative proceeding was void on the ground that Judge Elliot was acting as an "Officer of the United States" even though he had not been appointed under the Appointments Clause. Despite this Court's jurisprudence—instructing that an "Officer of the United States" is "'any appointee exercising significant authority pursuant to the laws of the United States,'" *Freytag*, 501 U.S. at 881 (quoting *Buckley v. Valeo*, 424 U.S. 1, 126 (1976))—a panel of the D.C. Circuit held that Judge Elliot was not an "Officer" within the meaning of the Appointments Clause. Pet. App. 9a-21a (disregarding *Freytag* and applying *Landry v. FDIC*, 204 F.3d 1125 (D.C. Cir. 2000)).

Other circuit courts have reached the opposite conclusion about the nature of the ALJ office. In *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016), the court held that an SEC administrative law judge was an "Officer" because, as in *Freytag*, (1) the position was "established by law," (2) the duties, salary, and means of appointment were specified by statute, and (3) the ALJ "'exercise[d] significant discretion' in 'carrying out . . . important functions.'" *Id.* at 1179-82.

In *Burgess v. FDIC*, 871 F.3d 297 (5th Cir. 2017), the court granted a stay after concluding that the

plaintiff had a likelihood of success on the merits in establishing that an ALJ of the FDIC is an officer of the United States. Following *Freytag* and *Bandimere*, the court concluded that a government worker is an "inferior Officer" under the Appointments Clause if the "office entails 'significan[t] . . . duties and discretion[,]'" a determination based on "(1) whether the office is 'established by Law;' (2) whether the 'duties, salary, and means of appointment for that office are specified by statute;' and (3) whether the officeholder may '"exercise significant discretion" in "carrying out . . . important functions."'" *Burgess*, 871 F.3d at 302 (citations omitted).

This case presents the Court with an issue going to the heart of our constitutional structure: May Congress authorize administrative law judges from an executive-branch agency to conduct adjudicatory proceedings without providing for the proper appointments of those judges? That is, does the Constitution allow Congress to create offices in the Executive Branch without also requiring for the appointment of officers under the Appointments Clause?

It also gives the Court an opportunity to reconsider whether its recent "significant authority" standard complies with the Constitution's demand for government accountability. The Founders' emphatic concern with despotism in the form of a multitude of unaccountable offices suggests that this Court's recent "significant authority" test should be reconsidered. The Court's earlier formulation—that an officer is any individual who has ongoing responsibility for a governmental duty—is consistent with the Constitution's text and history and protects

the Framers' intentions with respect to the Appointments Clause.

Ultimately, this Court should reverse the D.C. Circuit's opinion and hold that the SEC's administrative law judges are "Officers of the United States."

ARGUMENT

I. THE CONSTITUTION ESTABLISHED A GOVERNMENT OF SEPARATED POWERS TO PROTECT INDIVIDUAL LIBERTY

"No political truth is certainly of greater intrinsic value, or is stamped with the authority of more enlightened patrons of liberty," than this: "The accumulation of all powers, legislative, executive, and judiciary, in the same hands, whether of one, a few, or many, and whether hereditary, self-appointed, or elective, may justly be pronounced the very definition of tyranny." *The Federalist No. 47*, at 324 (James Madison) (J. Cooke ed. 1961).

To prevent tyranny, then, the Constitution divides the "powers of the . . . Federal Government into three defined categories, Legislative, Executive, and Judicial." *INS v. Chadha*, 462 U.S. 919, 951 (1983). Article I vests "[a]ll legislative Powers . . . in a Congress of the United States[;]" Article II vests "the" executive power "in a President of the United States of America[;]" and Article III vests "[t]he judicial Power of the United States . . . in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish." U.S. Const. art. I, § 1; art. II, § 1; art. III, § 1.

"The declared purpose of separating and dividing the powers of government, of course, was to 'diffus[e] power the better to secure liberty.'" *Bowsher v. Synar*, 478 U.S. 714, 721 (1986) (quoting *Youngstown Sheet & Tube Co. v. Sawyer*, 343 U.S. 579, 635 (1952) (Jackson, J., concurring)).

But the Framers knew that these mere "parchment barriers" between the branches were not a sufficient guarantor of liberty. *The Federalist No. 48*, at 333 (James Madison) (J. Cooke ed. 1961). Therefore, the Constitution also "give[s] to each [branch] a constitutional control of the others," without which "the degree of separation which the maxim requires, as essential to a free government, [could] never in practice be duly maintained." *Id.* at 332. The "constant aim," Madison explained, was "to divide and arrange the several [branches] in such a manner as that each may be a check on the other." *The Federalist No. 51*, at 349 (James Madison) (J. Cooke ed. 1961).

In sum, so that individual liberty may be secured, the Constitution divides power into three branches but also gives to each branch certain powers to check the others:

> [P]ower is of an encroaching nature, and . . . it ought to be effectually restrained from passing the limits assigned to it. After discriminating, therefore, in theory, the several classes of power, as they may in their nature be legislative, executive, or judiciary, the next and most difficult task is to provide some practical security for each, against the invasion of the others.

The Federalist No. 48, at 332 (James Madison) (J. Cooke ed. 1961). *See also Metro. Wash. Airports Auth.*, 501 U.S. at 272 ("The structure of our Government as conceived by the Framers of our Constitution disperses the federal power among the three branches—the Legislative, the Executive, and the Judicial—placing both substantive and procedural limitations on each.").

In particular, "because 'the power of appointment to offices' was deemed 'the most insidious and powerful weapon of eighteenth century despotism[,]'" "manipulation of official appointments had long been one of the American revolutionary generation's greatest grievances against executive power." *Freytag*, 501 U.S. at 883 (quoting Gordon S. Wood, *The Creation of the American Republic 1776-1787*, at 79, 143 (1969)).

Thus, the Appointments Clause—itself a microcosm of the Constitution's Separation of Powers.

II. WITHOUT STRICT ENFORCEMENT OF THE APPOINTMENTS CLAUSE, PUBLIC ACCOUNTABILITY AND INDIVIDUAL LIBERTY ARE THREATENED

A. The Appointments Clause Was Intended To Limit Both Executive and Legislative Power

The Appointments Clause "is among the significant structural safeguards of the constitutional scheme." *Edmond*, 520 U.S. at 659. It "embodies both separation of powers and checks and balances." *Bandimere*, 844 F.3d at 1172 (citation omitted). The Clause separates power by "defining unique roles for each branch in appointing officers." *Ibid.* And it

ensures checks and balances by preventing appointments without the cooperation of the Executive and Legislative branches. The President may appoint principal officers only upon Senate approval. U.S. Const. art. II, § 2, cl. 2. "Inferior Officers" may be appointed, upon congressional authorization, only by the President alone, the Heads of Departments, or the Courts of Law. *Id.*

Of course, under the Necessary and Proper Clause, Congress may create "offices" and establish their duties. *See Buckley*, 424 U.S. at 38. But the Constitution "does not contemplate an active role for Congress in the supervision of officers charged with the execution of the laws it enacts." *Bowsher*, 478 U.S. at 722. Once Congress has "ma[de] its choice in enacting legislation, its participation ends. Congress can thereafter control the execution of its enactment only indirectly—by passing new legislation." *Id.* at 733-34 (citing *Chadha*, 462 U.S. at 958). *See also Freytag*, 501 U.S. at 880 (The Appointments Clause "prevents Congress from dispensing power too freely; it limits the universe of eligible recipients of the power to appoint."); *Free Enterprise Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 516 (2010) (Breyer, J., dissenting) (The separation-of-powers "principle, along with the instruction in Article II, § 3 that the President 'shall take Care that the Laws be faithfully executed,' limits Congress' power to structure the Federal Government."); *Myers v. United States*, 272 U.S. 52, 163-64 (1926) ("[A]rticle 2 grants to the President the executive power of the government—*i.e.*, the general administrative control of those executing the laws, including the power of appointment and removal of executive officers—a

conclusion confirmed by his obligation to take care that the laws be faithfully executed.").

But here, Congress has avoided the strictures of the Appointments Clause by granting to the agents of administrative agencies vast authority without designating those employees as "Officers" within the meaning of the Appointments Clause.[2] In this way, Congress has "'mask[ed], under complicated and indirect measures, the encroachments which it makes on the co-ordinate departments,' *[The Federalist] No. 48*, p. 310 [(C. Rossiter ed. 1961)] (J. Madison), and thus control[s] the nominal actions (*e.g.*, appointments) of the other branches." *Freytag*, 501 U.S. at 906 (Scalia, J., concurring in part and concurring in the judgment) (citing Thomas Jefferson, *Notes on the State of Virginia* 120 (William Peden ed. 1955)).

And by thus removing from the President (or department heads or courts of law) the power to appoint officers, Congress has arrogated to itself significant Executive power—a danger the Framers sought to prevent. *See Chadha*, 462 U.S. at 947 (explaining that the Framers recognized the particular "'propensity'" of the legislative branch "'to invade the rights of the Executive'") (quoting *The Federalist No. 73*, at 494 (Alexander Hamilton) (J. Cooke ed. 1961). *See also Ryder v. United States*, 515 U.S. 177, 182 (1995) (The Appointments Clause is a

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[2] As Petitioners note, Congress refers to the SEC's administrative law judges as "officers." *See* Pet. Br. 3. But Congress does not require that these "officers" be appointed under the Appointments Clause.

"bulwark against one branch aggrandizing its power at the expense of another branch.").

B. The Appointments Clause Was Also Intended To Limit the Diffusion of the Appointment Power To Protect the Governed and Increase Accountability

The limits set forth in the Appointments Clause do not exist simply to settle inter-branch squabbles over control of the government. Rather, these limitations go to the heart of a self-governing people. As the Framers understood, "by limiting the appointment power, they could ensure that those who wielded it were accountable to political force and the will of the people." *Freytag*, 501 U.S. at 884. And the appointment of "Officers" under the Appointments Clause was one means of holding the President accountable: the President is "directly dependent on the people, and since there is only *one* President, *he* is responsible. The people know whom to blame." *Morrison v. Olson*, 487 U.S. 654, 729 (1988) (Scalia, J., dissenting).

Whom should Mr. Lucia blame? He and his (former) company were subjected to a proceeding affecting his fundamental right to pursue an avocation. *See Cummings v. Missouri*, 71 U.S. 277, 321-22 (1866). This proceeding, however, was initiated by agents of the SEC and overseen by another agent of the SEC. And the ALJ who presided over this proceeding wielded significant authority—permanently barring Mr. Lucia from working as an investment adviser—despite not having been appointed under the Appointments Clause. Is Congress to blame for establishing this administrative process? Or is the President

accountable for administering the laws against Petitioners? Mr. Lucia, and others facing the ever-growing Administrative State, should not have to guess whom to hold accountable. *See Ass'n of Am. R.R.s*, 135 S. Ct. at 1234 (Alito, J., concurring) ("Liberty requires accountability."). *See also Free Enterprise Fund*, 561 U.S. at 499 ("Our Constitution was adopted to enable the people to govern themselves, through their elected leaders. The growth of the Executive Branch, which now wields vast power and touches almost every aspect of daily life, heightens the concern that it may slip from the Executive's control, and thus from that of the people.").

Indeed, precisely because bureaucracy is the "ultimate black box of government—the place where exercises of coercive power are most unfathomable and thus most threatening[. . .]—the need for transparency, as an aid to holding governmental decisionmakers to account, here reaches its apex." Kagan, *supra*, at 2332.

This Court should reverse the opinion below and reinforce the doctrine of Separation of Powers, which was established to protect the people's liberties and ensure justice. *See Freytag*, 501 U.S. at 870 ("The leading Framers of our Constitution viewed the principle of separation of powers as the central guarantee of a just government.").

III. THIS CASE SHOWS THE DANGER OF UNACCOUNTABLE GOVERNMENT AND THE GROWING THREAT OF THE ADMINISTRATIVE STATE

A. The SEC's ALJs Exercise "Significant Authority" and, Therefore, They Are Inferior Officers Subject to the Appointments Clause

Freytag and *Buckley* require the reversal of the D.C. Circuit's opinion. According to those cases, an "Officer of the United States" is "'any appointee exercising significant authority pursuant to the laws of the United States,'" and they "'must, therefore, be appointed in the manner prescribed by'" the Appointments Clause. *Freytag*, 501 U.S. at 881 (quoting *Buckley*, 424 U.S. at 126). In *Freytag*, this Court concluded that the office of "special trial judge" within the U.S. Tax Court had been "established by Law" (the "duties, salary, and means of appointment for that office are specified by statute"); and that these special trial judges exercised significant discretion in carrying out their "important functions" (taking testimony, conducting trials, ruling on admissibility of evidence, and having power to enforce compliance with discovery orders). *Id.*, 501 U.S. at 881-82. Further, because of these "significant" authorities, the judges' inability to enter final decisions was not, contrary to the D.C. Circuit's opinion, dispositive. *Ibid.* Therefore, special trial judges are "inferior Officers" within the meaning of the Appointments Clause.

The same conclusion applies to the SEC's ALJ here. Congress not only refers to SEC ALJs as "officers of the Commission," 15 U.S.C. §§ 77u, 78v, 80a-40,

80b-12, but Congress has also established their duties and salary by law, 5 U.S.C. §§ 556-557 (duties), 5372(b) (salary). Further, as noted above, Administrative Law Judge Cameron Elliot exercised "significant authority" in the proceeding at issue: he heard testimony, including expert-witness testimony; ruled on the admissibility of evidence; considered and ruled on objections; weighed evidence; made factual findings; reached legal conclusions; permanently barred Mr. Lucia from working as an investment advisor; revoked his (former) company's registration, and imposed civil penalties in the amount of $300,000. Pet. App. 115a-237a (ALJ Initial Decision on Remand). Accordingly, the Court should hold that SEC ALJs are inferior officers, subject to the Appointments Clause.

B. This Court Should Reconsider Its "Significant Authority" Test, Which Is Inconsistent with the Constitution and This Court's Early Jurisprudence

1. The Expanding Administrative State Requires Accountability

Mr. Lucia's predicament is, of course, just one example of the threat posed to individual liberty by an unaccountable Administrative State.[3] Congress's unilateral establishment of offices, which Congress intended to be filled outside of the Appointments Clause, creates the very dangers that the Framers sought to avoid: the diffusion of the appointment power and the accompanying decrease in

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[3] Mr. Lucia's administrative odyssey began in 2012, when the SEC initiated its enforcement action. Pet. App. 116a. He has lost his company and is near bankruptcy. Pet. Br. 58.

accountability. As the Administrative State expands, these concerns only grow, because of the increased likelihood that its power "slip[s] from the Executive's control, and thus from that of the people." *Free Enterprise Fund*, 561 U.S. at 499.

To be sure, a reversal of the D.C. Circuit's opinion will be a step in the right direction: requiring that SEC ALJs be appointed under the Appointments Clause will limit the diffusion of appointment power and increase the accountability for the ALJs' actions. But this step does not go far enough—as the circuit courts' disparate understandings of "significant authority" demonstrates. This Court should take this opportunity to reconsider that "significant authority" standard, which still allows Congress and the President to avoid the Appointments Clause and staff the Administrative State with millions of employees who can "wield[] vast power" over "almost every aspect of daily life." *Free Enterprise Fund*, 561 U.S. at 499.

2. An Employee Need Not Exercise "Significant" Authority To Be an "Officer" Under the Appointments Clause

A definition of "officer" that is faithful to the Constitution and this Court's earlier jurisprudence is as follows: any federal employee who has "ongoing responsibility for a governmental duty." Jennifer L. Mascott, *Who Are "Officers of the United States?"*, 70 Stan. L. Rev. 443, 450 (2018) (footnote omitted).

This definition would necessarily result in the recognition of more offices that must be filled (only) through the Appointments Clause. But any resulting

"inconvenience" creates no *constitutional* difficulty. As this Court stated long ago, the appointment of principal officers "requires a nomination by the President and confirmation by the Senate. But *foreseeing that when offices became numerous*, and sudden removals necessary, this mode might be inconvenient," the Constitution provided Congress with the authority to vest the power to appoint inferior officers in the President alone, in the courts of law, or in the heads of departments. *United States v. Germaine*, 99 U.S. 508, 509-10 (1878) (emphasis added).[4]

Further, *Germaine* and other early cases support the broad, "non-significant authority" definition suggested above. In *United States v. Hartwell*, 73 U.S. (6 Wall.) 385 (1867), for example, this Court held that an "office" is a "public station, or employment,

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[4] Thus, the Appointments Clause itself provides a more convenient method to appoint inferior officers: The "obvious purpose" in authorizing Congress to vest appointment power of "inferior Officers" in the President alone, in the Courts of Law, or in the Heads of Departments, is "administrative convenience." *Edmond*, 520 U.S. at 660 (citing *Germaine*, 99 U.S. at 510). But the Constitution permits no further "convenience."

More generally, as this Court has repeatedly affirmed, "'that a given law or procedure is efficient, convenient, and useful in facilitating functions of government, standing alone, will not save it if it is contrary to the Constitution,'" for "'[c]onvenience and efficiency are not the primary objectives—or the hallmarks—of democratic government.'" *Free Enterprise*, 561 U.S. 499 (citations omitted). *See also Chadha*, 462 U.S. at 959 (explaining that there is "no support in the Constitution or decisions of this Court for the proposition that the cumbersomeness and delays often encountered in complying with explicit Constitutional standards may be avoided, either by the Congress or by the President.").

conferred by the appointment of government. The term embraces the ideas of tenure, duration, emolument, and duties." *Id.* at 393. Notably, *Hartwell's* formulation does not include a requirement that an employee exercise "significant" authority before being an Officer of the United States:

> The employment of the defendant was in the public service of the United States. He was appointed pursuant to law, and his compensation was fixed by law. Vacating the office of his superior would not have affected the tenure of his place. His duties were continuing and permanent, not occasional or temporary. They were to be such as his superior in office should prescribe.

Ibid.

According to *Germaine*, "officers" means "all persons who can be said to hold an office under the government" of the United States. *Id.*, 99 U.S. at 510. And it relied on *Hartwell* when it identified the "nature" of the employment that makes it an "office": tenure, duration, emolument, and duties. *Germaine*, 99 U.S. at 511 (citing *Hartwell*).

As these cases show, the key factor in determining whether an employee is an Officer of the United States is whether that employee has a *duty* to carry out a function (of the federal government). *See* Mascott, *supra*, at 463 (The "application of [a duty] standard in fact is consistent with the outcome of numerous Supreme Court decisions evaluating

Article II officer status.") (footnote omitted).[5] The duty or duties of an officer must be ongoing and established by law, of course. *See Freytag*, 501 U.S. at 881 (noting that the office of special trial judge was "'established by Law,' Art. II, § 2, cl. 2, and the duties, salary, and means of appointment for that office are specified by statute.") (citing *Burnap v. United States*, 252 U.S. 512, 516-17 (1920), and *Germaine*, 99 U.S. at 511-12).

But the duties need *not* be significant.

The *Bandimere* opinion was thus able to identify numerous positions, involving less-than-significant responsibilities, previously held to be "Officers" by this Court:

- a district court clerk, *Ex parte Hennen*, 38 U.S. (13 Pet.) 230, 258 (1839);
- an "assistant-surgeon," *United States v. Moore*, 95 U.S. 760, 762 (1877);

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[5] As Mascott explains, the "element of duty was significant to the outcome" of *Germaine*: "[T]he official under consideration had only 'occasional and intermittent' duties; thus he was not an officer. The Court expressed no concern with whether the relevant duties were significant or involved discretion or final decisionmaking power. Rather, the opinion seemed to intimate that if the relevant official had maintained 'continuing and permanent' duties, the Court would have considered him an Article II officer." *Id.*, *supra*, at 463 (footnotes omitted).

The importance of an employee's duty was recognized at common law. *See* Edward S. Corwin, *The President: Office and Powers 1789-1948*, at 83 (3d ed. 1948) ("Etymologically, an 'office' is an *officium*, a duty; and an 'officer' was simply one whom the King had charged with a duty.").

- "thousands of clerks in the Departments of the Treasury, Interior, and the othe[r]" departments, *Germaine*, 99 U.S. at 511;
- an election supervisor, *Ex parte Siebold*, 100 U.S. 371, 397-98 (1879);
- a "cadet engineer" appointed by the Secretary of the Navy, *United States v. Perkins*, 116 U.S. 483, 484-85 (1886);
- a United States commissioner in district court proceedings, *Go-Bart Importing Co. v. United States*, 282 U.S. 344, 352-54 (1931); [and]
- a postmaster first class, *Buckley*, 424 U.S. at 126 (citing *Myers v. United States*, 272 U.S. 52 (1926));

Bandimere, 844 F.3d at 1173-74; *see id.* at 1174 (collecting additional examples). *See also* William Blackstone, 3 *Commentaries on the Laws of England* 327-46 (1765) (An "officer" includes "sheriffs; coroners; justices of the peace; constables; surveyors of highways; and overseers of the poor."); Mascott, *supra*, at 450 (Traditionally, officers have "included even individuals with more ministerial duties like recordkeeping.") (footnote omitted).

3. Buckley's "Significant Authority" Standard Was Not Well Considered

In *Buckley*, the Court relied on language from the *Germaine* opinion in adopting its "significant authority" rule. *Germaine* explained that officers are

"all persons who can be said to hold an office." *Id.*, 99 U.S. at 510. *Buckley* used this precise language: "We think that the term 'Officers of the United States' as used in Art. II, [is] defined to include 'all persons who can be said to hold an office under the government,'" *Buckley*, 424 U.S. at 125-26 (quoting *Germaine*, 99 U.S. at 510). But *Buckley* continued in a cursory manner.

According to *Buckley*, the term "Officers of the United States" is "intended to have substantive meaning[,]" and the term's "import is that any appointee exercising *significant* authority pursuant to the laws of the United States" is an "Officer of the United States." *Buckley*, 424 U.S. at 126 (emphasis added). *Buckley* did not define "significant," nor did it explain why the "fair" import of the term "Officers of the United States" requires an employee's exercise of "significant" authority.[6]

Indeed, the very next paragraph in *Buckley* undermines the Court's inference. There, the Court supported its conclusion—that FEC commissioners were inferior officers—by comparing those offices to the offices of postmaster first class and a district-court clerk, both of which were held by this Court to be inferior officers under the Appointments Clause. *Id.*, 424 U.S. at 126 (citing *Myers*, *supra*, 272 U.S. 52, and *Ex parte Hennen*, 38 U.S. 225 (1839)). But it seems quite unlikely that either a postmaster first class or a district-court clerk would meet the "significant authority" standard.

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[6] In *Freytag*, the Court quoted this language from *Buckley* but likewise did not define "significant." *See Freytag*, 501 U.S. at 881 (quoting *Buckley*, 424 U.S. at 126).

Further, *Buckley*'s stated distinction between officers and "mere" employees similarly lacks support from the cited authorities. According to *Buckley*, non-officer employees are "lesser functionaries subordinate to officers of the United States." *Id.*, 424 U.S. at 126 n.162 (citing *Auffmordt v. Hedden*, 137 U.S. 310, 327 (1890), and *Germaine*, *supra*).[7] But neither *Auffmordt* nor *Germaine* holds that "mere" employees cannot be officers.

As noted above, in *Germaine*, the Court explained that the term "office" "embraces the ideas of tenure, duration, emolument, and duties, and that the latter were continuing and permanent, not occasional or temporary." *Id.*, 99 U.S. at 511-12. The Court held that a surgeon was not an officer because his "duties [we]re *not* continuing and permanent, and they *[we]re* occasional and intermittent[;]" he acted "only . . . when called on by the Commissioner of Pensions in some special case[;]" he was "required to keep no place of business for the public use[;]" and "[n]o regular appropriation [wa]s made to pay his compensation." *Id.* But *Germaine* "expressed no concern with whether the relevant duties were significant or involved discretion or final decisionmaking power[,]" Mascott, *supra*, at 463, and *Germaine* therefore fails to show that a "lesser functionary" is—solely because of his presumed insignificant duties—a "mere," non-officer employee.

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[7] *Freytag* relied on this language. See *id.*, 501 U.S. at 880 (addressing whether "a special trial judge is only an employee," since "such 'lesser functionaries' need not be selected in compliance with the strict requirements of Article II") (citing *Buckley*, 424 U.S. at 126, n.162). Again, *Freytag* did not define the meaning of "lesser functionary."

Similarly, *Auffmordt* held that a "merchant appraiser" was not an officer because he was not a full-time employee, he was "selected for the special case[,]" and because he had "no general functions, nor any employment which ha[d] any duration as to time, or which extend[ed] over any case further than as he [wa]s selected to act in that particular case." *Id.*, 137 U.S. at 326-27. In short, the appraiser's position was "without tenure, duration, continuing emolument, or continuous duties, and he act[ed] only occasionally and temporarily." *Id.* at 327.

Auffmordt cited to several opinions that likewise allow for a "mere" employee to be an officer—so long as the employee acted "with[] tenure, duration, continuing emolument, or continuous duties, and act[ed] [not] occasionally and temporarily." *Ibid. See ibid.* (citing *United States v. Maurice*, 26 F. Cas. 1211, 1214 (Va. Cir. Ct. 1823) (Marshall, J.) (identifying nature of an officer as one with a "continuing" duty "defined by rules prescribed by the government, and not by contract," who has (non-contractual) duties that "continue, though the person be changed"); *Hartwell*, 73 U.S. at 393 ("The term ['office'] embraces the ideas of tenure, duration, emolument, and duties.") (holding that a clerk to an assistant treasurer in Boston was an officer); *Germaine*, 99 U.S. at 510, 511; *Hall v. Wisconsin*, 103 U.S. 5, 8 (1880) (The term "office" "embraces the ideas of tenure, duration, emolument, and duties, and that the latter were continuing and permanent, not occasional or temporary.")).[8]

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[8] *Auffmordt* also cited *United States v. Smith*, 124 U.S. 525, 532 (1888), and *United States v. Mouat*, 124 U.S. 303, 307 (1888), but

Thus, contrary to *Buckley*'s apparent reading of this Court's earlier jurisprudence, this Court has held that "mere" employees can be officers as that term is used in the Appointments Clause. *See, e.g., Germaine*, 99 U.S. at 511 (describing, as officers, "thousands of clerks in the Departments of the Treasury, Interior and the othe[r]" departments responsible for "the records, books, & papers appertaining to the office").

4. Buckley Can Be Read Consistently with the Court's Early Case-Law

Perhaps *Buckley's* rather conclusory statements concerning "significant authority" and the purported distinction between officers and employees can be understood as *reaffirming* the Court's long-standing interpretation of the Appointments Clause. Thus, it is possible to read *Buckley* as saying that "significant authority" means "sovereign authority." *See, e.g.*, Kevin Sholette, Note, *The American Czars*, 20 Cornell J.L. Pub. Pol'y 219, 230 (2010) (arguing that *Buckley* "did not intend to depart from the historical understanding of what constitutes a public office[,]" and that therefore, "the phrase 'significant authority' is best understood as expressing the idea that exercising any 'sovereign authority' is a significant duty") (footnote omitted). *See id.* at 235 ("[T]he best definition for a federal 'officer' is someone vested with the duty of exercising sovereign authority of the United States, for the benefit of the public, except where that duty is only contractual, personal, or only occasional and intermittent."). *See also The Federalist*

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these case did not address the nature of an "officer." Rather, they held that a person who was not appointed under Appointments Clause cannot be an officer.

No. 72, at 487 (Alexander Hamilton) (J. Cooke ed. 1961) (explaining that persons "to whose immediate management [executive functions] are committed, ought to be considered as the assistants or deputies of the chief magistrate; and, on this account, they ought to derive their offices from his appointment").

A 2007 opinion from the Office of Legal Counsel supports this reading. *See* Officers of the U.S. Within the Meaning of the Appointments Clause, 31 Op. O.L.C. 73 (2007). The OLC concluded that "a position, however labeled, is in fact a federal office if (1) it is invested by legal authority with a portion of the *sovereign* powers of the federal government, and (2) it is 'continuing.'" *Id.* at 73-74 (emphasis added). Recall that *Germaine* defined "officers" as "all persons who can be said to hold an office *under the government" of the United States*. *Id.*, 99 U.S. at 510 (emphasis added).

This reading is also supported by the historical foundations of the Nation and the Framers' fears of the diffusion of appointment power and the resulting decrease in accountability.

Among the Revolutionaries' charges against George III was that he had "erected a multitude of new Offices, and sent hither swarms of Officers to harass our people and eat out their substance." Declaration of Independence (U.S. 1776). At the Revolution, most Americans worried about excessive power in the executive. *See Freytag*, 501 U.S. at 883 ("[B]ecause 'the power of appointment to offices' was deemed 'the most insidious and powerful weapon of eighteenth century despotism[,]'" "manipulation of official appointments had long been one of the American revolutionary generation's greatest

grievances against executive power.") (quoting Gordon S. Wood, *The Creation of the American Republic 1776-1787*, at 79, 143 (1969)). But by the time the Constitution had been drafted, Americans became concerned that despotism could arise from the Legislative Branch as well. *See, e.g., The Federalist No. 51*, at 351 (James Madison) (J. Cooke ed. 1961) ("If a majority be united by a common interest, the rights of the minority will be insecure.").

Does it matter whether the multitude of new offices includes only *significant* offices? Is it reasonable to suppose that the Framers objected to swarms of harassing officers only if they possessed *significant* authority? Cannot "swarms" of "mere" employees harass the people and eat out their substance with less than *significant* authority?

Further, as *Freytag* notes, the Appointments Clause "not only guards against th[e] encroachment [of one branch's power by another,] but also preserves another aspect of the Constitution's structural integrity by preventing the diffusion of the appointment power." *Id.*, 501 U.S. at 878. Would the Framers have intended for Congress (or the President) to be able to evade this structural concern through the pretext of establishing *insignificant* offices, to be staffed by *insignificant* employees? *See id.* at 880 (The Appointments Clause "prevents Congress from dispensing power too freely; it limits the universe of eligible recipients of the power to appoint."); *Hartwell*, 73 U.S. (6 Wall.) at 393 (An "office" is a "public station, or employment, conferred by the appointment of government.").

To the contrary, staffing the Administrative State must be done with clear accountability in mind:

> The diffusion of power carries with it a diffusion of accountability. The people do not vote for the "Officers of the United States." Art. II, § 2, cl. 2. They instead look to the President to guide the "assistants or deputies ... subject to his superintendence." *The Federalist No. 72*, p. 487 (J. Cooke ed. 1961) (A. Hamilton). Without a clear and effective chain of command, the public cannot "determine on whom the blame or the punishment of a pernicious measure, or series of pernicious measures ought really to fall." *Id.*, No. 70, at 476 (same). That is why the Framers sought to ensure that "those who are employed in the execution of the law will be in their proper situation, and the chain of dependence be preserved; the lowest officers, the middle grade, and the highest, will depend, as they ought, on the President, and the President on the community." 1 Annals of Cong., at 499 (J. Madison).

Free Enterprise Fund, 561 U.S. at 497-98. *See also Ass'n of Am. R.R.s*, 135 S. Ct. at 1234 (Alito, J., concurring) (arguing that the Appointments Clause "ensures that those who exercise the power of the United States are accountable to the President, who himself is accountable to the people." (citing *Free Enterprise Fund*, 561 U.S. at 497-98)); *Buckley*, 424 U.S. at 271 (White, J., concurring in part and dissenting in part) ("The appointment power was a major building block fitted into the constitutional structure designed to avoid the accumulation or

exercise of arbitrary power by the Federal Government.").

As *Buckley* recognized, "*all* officers of the United States are to be appointed in accordance with the Clause. . . . No class or type of officer is excluded because of its special functions." *Id.*, 424 U.S. at 132. Thus, the "prescribed manner of appointment for principal officers is also the default manner of appointment for inferior officers." *Edmond*, 520 U.S. at 660. This suggests that the "significance" of a position's authority is not a dispositive factor in determining whether a position in the federal government is an "office" subject to the Appointments Clause. Rather, as this Court has explained, "in the context of a Clause designed to preserve political accountability relative to important Government assignments, we think it evident that 'inferior officers' are officers whose work is directed and supervised at some level by others who were appointed by Presidential nomination with the advice and consent of the Senate." *Id.* at 663.

Thus, a return to the broad, duty-based standard of "Officer" would increase the accountability of the modern Administrative State. If Congress had to identify the means for the appointment of any employee with ongoing responsibility for a statutory duty under the federal government, it would likely engage in more careful consideration before creating "offices" and "officers." And the President would unmistakably bear the responsibility—and could not

pass the buck—for the conduct of all "officers" within the Executive Branch.[9]

The Court's more-recent formulation—that an "Officer of the United States" is "any appointee exercising significant authority pursuant to the laws of the United States," *Buckley*, 424 U.S. at 126—ignores the common-sense statement in *Germaine* ("officers" means "all persons who can be said to hold an office under the government" of the United States, *id.*, 99 U.S. at 510); the early practice in our Nation's history; as well as the central theme of the separation of powers, namely, that the government must be accountable to the governed.

If Congress and the President can now staff the Executive Branch—outside the strictures of the Appointments Clause—with individuals who are accountable to neither the President nor the public, on the ground that only those employees who exercise some kind of "significant" authority are subject to the Appointments Clause, then the Framers' goals of separation of powers, checks and balances, and

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[9] While the Court has distinguished between officers and employees, "[i]t is certainly conceivable, perhaps even likely, that the Framers of the Constitution conceived only two classes of federal employ—the Officers and the inferior Officers." John M. Burkoff, *Appointment and Removal under the Federal Constitution: The Impact of* Buckley v. Valeo, 22 Wayne L. Rev. 1335, 1338 (1976); *see id.* n.10 (noting that in 1973, the federal government's more than 14,000,000 employees represented 19% of all employment, while in 1801 the federal government had only 2,100 employees). *Cf. also* James Madison, 1 Annals of Cong. 463 (1789) ("[I]f any power whatsoever is in its nature Executive, it is the power of appointing, overseeing, and controlling those who execute the laws.").

accountable government are threatened, if not defeated.

* * *

While it may be possible to rule that Mr. Lucia should prevail even under the significant-authority standard, such a ruling would not solve the broader problems raised by Mr. Lucia's case. Indeed, Mr. Lucia's dilemma shows that the aggressive and growing Administrative State must be held more accountable. This accountability requires a return to the traditional understanding of "officer" as any federal employee with ongoing responsibility for a governmental duty. Accordingly, the Court should re-adopt the traditional definition of "officer" to protect the individual liberty and governmental accountability that lie at the heart of our Constitution generally and the Appointments Clause specifically.

CONCLUSION

The "purpose of the separation and equilibration of powers in general, and of the unitary Executive in particular, was not merely to assure effective government but to preserve individual freedom." *Morrison*, 487 U.S. at 654 (Scalia, J., dissenting). And the "hydraulic pressure inherent within each of the separate Branches to exceed the outer limits of its power, even to accomplish desirable objectives, must be resisted." *Chadha*, 462 U.S. at 951. While each branch's interpretation of its own powers is entitled to "great respect," in the end, "'[i]t is emphatically the province and duty of the judicial department to say what the law is.'" *United States v. Nixon*, 418 U.S. 683, 703 (1974) (quoting *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 177 (1803)).

With these precepts in mind, this Court should reverse the opinion of the D.C. Circuit and hold that SEC administrative law judges are officers of the United States whose positions are subject to the strictures of the Appointments Clause. And to ensure accountability in the future, the Court should return to the traditional understanding of "officer" as any federal employee with ongoing responsibility for a sovereign, governmental duty.

DATED: February 27, 2018.

Respectfully submitted,

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No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, *et al.*,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DC CIRCUIT

BRIEF OF RD LEGAL CAPITAL, LLC AND RONI DERSOVITZ AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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INTEREST OF *AMICI CURIAE*[1]

Amicus Curiae RD Legal Capital, LLC ("RDLC"), is a management firm for two hedge funds (the "Funds") launched by *Amicus Curiae* Roni Dersovitz ("Mr. Dersovitz" and, together with RDLC, the "RDLC *Amici*") to raise capital for investments in legal financing. As described in the Funds' offering documents, the Funds seek to generate stable returns for investors, while maintaining capital, through: (a) purchasing from law firms their receivables for legal fees owed; (b) purchasing from plaintiffs their receivables for proceeds from legal judgments or settlements; (c) providing loans to law firms through secured lines of credit; and (d) providing capital to law firms to pursue certain other opportunities that do not fall within the foregoing categories. Since their inception, the Funds have financed and successfully collected more than $400 million spread over more than 2,300 positions originated from attorneys and plaintiffs, and the Funds' wealthy, accredited investors have correspondingly earned compounded double-digit annual returns on their investments.

In March 2015, the Securities and Exchange Commission (the "SEC" or "Commission") began an investigation into whether RDLC and Mr. Dersovitz violated the anti-fraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934. The

1. Pursuant to Supreme Court Rule 37.3, *amici* certify that all parties have consented to the filing of this brief. Pursuant to Rule 37.6, *amici* certify that no counsel for a party authored this brief in whole or in part, and no persons other than *amici* or their counsel made a monetary contribution to its preparation or submission.

investigation focused largely on the Funds' investments in assets related to certain receivables arising from a series of consolidated judgment enforcement cases captioned as *Peterson v. Islamic Republic of Iran*, No. 10 Civ. 4518 (KBF), 2013 WL 1155576 (S.D.N.Y. Mar. 13, 2013), *aff'd by Bank Markazi v. Peterson*, 136 S. Ct. 1310, 1317 (2016) ("*Peterson*"). During the investigation, Mr. Dersovitz explained consistently and in detail that he operated within the parameters of the Funds' operating documents, always disclosed the investments in *Peterson*—which he consistently described to investors as the "best trade in the book"—and had the discretion and flexibility to invest heavily in such a strong trade. Moreover, *no investor in the Funds lost any money* in connection with the *Peterson* trades (or any other).

Even though investors profited handsomely from investing in the Funds, the Commission initiated an administrative proceeding against the RDLC *Amici* by filing an Order Instituting Administrative and Cease-and-Desist Proceedings ("OIP") on July 14, 2016. *See In the Matter of RD Legal Capital, LLC and Roni Dersovitz*, Administrative Proceeding File No. 3-17342 (July 14, 2016).[2] The proceeding culminated in an administrative hearing before an SEC administrative law judge ("ALJ") that lasted five weeks, involved 43 witnesses, and generated a transcript 7,214 pages long, along with 1,059 individual exhibits. The post-trial briefing involved multiple motions—including on constitutional grounds—and a request by the Commission's Division of

2. All orders from the RDLC *Amici*'s administrative enforcement proceeding are available at https://www.sec.gov/litigation/apdocuments/ap-3-17342.xml.

Enforcement (the "Division of Enforcement") for the SEC ALJ to make factual and credibility findings contained in a 406-page document, consisting of 741 proposed facts, hundreds of sub-facts, and 1,301 factual footnotes. For all intents and purposes, the hearing proceeded as if it were a bench trial presided over by a federal judge.

On August 16, 2017, the SEC ALJ issued an order granting the RDLC *Amici*'s motion for judgment as a matter of law, dismissing the Division of Enforcement's baseless claim that the RDLC *Amici* inappropriately valued the Funds' assets. The SEC ALJ has yet to issue an Initial Decision on the remaining allegations against the RDLC *Amici*.

At multiple stages of the process, the RDLC *Amici* raised constitutional challenges to the administrative proceeding:

- During the pre-hearing phase, the RDLC *Amici* brought a motion to dismiss the administrative proceeding, in part on the ground that SEC ALJs are inferior officers who were not appointed in accordance with the Appointments Clause. The RDLC *Amici*'s Appointments Clause challenge was rejected by the SEC ALJ, however, based on Commission precedent that had consistently (and erroneously) determined that SEC ALJs are mere employees rather than executive officers.

- The RDLC *Amici* also filed a federal action challenging the constitutionality of their administrative proceeding based, *inter alia*, on the Appointments Clause, but the United States

District Court for the District of New Jersey dismissed their complaint on jurisdictional grounds, accepting the Commission's argument that meaningful judicial review of the Appointments Clause issue was available through the administrative process. *See RD Legal Capital, LLC v. SEC*, United States District Court for the District of New Jersey, Case No. 2:16-5104, Order (ECF No. 23), Oct. 20, 2016 (relying on *Jarkesy v. SEC*, 803 F.3d 9, 16 (D.C. Cir. 2015), *Bebo v. SEC*, 799 F.3d 765, 767 (7th Cir. 2015), *Tilton v. SEC*, 824 F.3d 276, 291 (2d Cir. 2016), and *Hill v. SEC*, 825 F.3d 1236, 1252 (11th Cir. 2016)).

- The RDLC *Amici* filed a post-hearing brief in their administrative proceeding that again argued that the SEC ALJ presiding over their proceeding is an officer within the meaning of the Appointments Clause, but had not been constitutionally appointed. While that motion was pending, the Commission reversed its position on the constitutional status of its ALJs, and now agrees that its ALJs are executive officers and not mere employees. On November 30, 2017, however, the Commission purported to ratify the prior appointment of its ALJs in a misguided attempt to "put to rest" any Appointments Clause challenge. *See* Order, *In re Pending Administrative Proceedings*, Securities Act Release No. 10,440, 2017 WL 5969234, at *1 (Nov. 30, 2017) ("Ratification Order").

- The RDLC *Amici* then filed briefs before the SEC ALJ arguing, *inter alia*, that the Ratification Order did not cure the Appointments Clause

> infirmity. On February 23, 2018, however, the SEC ALJ issued an order stating that the Commission's Ratification Order cured any Appointments Clause infirmity. *See RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 5625 (ALJ Feb. 23, 2018).

Thus, like Petitioners before them, the RDLC *Amici* are respondents in an administrative proceeding presided over by an SEC ALJ who has exercised significant authority and whose hiring violates the Appointments Clause of the United States Constitution. The RDLC *Amici* accordingly have a direct and substantial interest in the outcome of this case, and urge the Court to conclude that: (1) SEC ALJs are "Officers of the United States" within the meaning of the Appointments Clause, but were not appointed in conformity with the Appointments Clause; and (2) the Commission cannot cure the Appointments Clause violations by "ratifying" the unconstitutional delegation of its responsibility to appoint SEC ALJs, or by asking SEC ALJs to reconsider and ratify decisions on their own constitutional status that they made prior to being appointed in a constitutional manner.

SUMMARY OF ARGUMENT

Prior to the passage in 2010 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), the Commission was statutorily prohibited from bringing administrative proceedings seeking financial penalties against unregistered entities such as the RDLC *Amici*, and was required to pursue those penalties against unregistered entities in federal court. While Dodd-Frank lifted that legislative restriction, it did not and

could not eliminate the constitutional infirmities of SEC administrative proceedings presided over by SEC ALJs who were not appointed in the manner prescribed by the Appointments Clause in Article II of the United States Constitution.

SEC ALJs perform functions and exercise responsibilities akin to federal judges presiding over bench trials. SEC ALJs make important pretrial rulings, control the discovery process, and have considerable discretion over whether to permit dispositive motions. SEC ALJs, moreover, are charged with admitting and distilling the evidence, and making factual and credibility findings, to compile an administrative record that, even if appealed, is afforded considerable deference. SEC ALJs thus control virtually every aspect of the administrative proceedings over which they preside. The administrative proceeding against the RDLC *Amici* is a case in point.

In Section I of this brief, the RDLC *Amici* provide an account of the SEC administrative proceeding against them to illustrate that SEC ALJs do, in fact, exercise significant authority that has a profound impact on litigants and on the financial viability of small businesses like RDLC. It is evident from the RDLC *Amici*'s case (and other such cases) that SEC ALJs exercise the kind of governmental authority that makes them executive officers subject to the Appointments Clause.

In Section II, the RDLC *Amici* explain that the Commission's belated attempt to unwind its constitutional violations by "ratifying" the process by which its ALJs were hired by the SEC's Chief ALJ distorts the ratification doctrine and runs counter to the non-delegable mandate

of the Appointments Clause. *See Buckley v. Valeo*, 424 U.S. 1, 118, 125-26 (1976) (per curiam) (the Appointments Clause establishes the "*exclusive* method by which those charged with executing the laws of the United States may be chosen") (emphasis added). Similarly, the Commission's instruction that its ALJs revisit and ratify actions that they took in pending administrative proceedings prior to being constitutionally appointed cannot remove the unconstitutional stain from those proceedings.

ARGUMENT

I. SEC ALJS EXERCISE "SIGNIFICANT AUTHORITY" OVER EVERY PHASE AND FACET OF AN SEC ADMINISTRATIVE PROCEEDING

Before the Court is the question of whether SEC ALJs are "Officers of the United States" within the meaning of the Appointments Clause in Article II of the Constitution. Although a deadlocked *en banc* panel of the D.C. Circuit in this case upheld an earlier panel opinion answering that question in the negative, *every other federal court* to have considered the question has held that SEC ALJs are "Officers of the United States" subject to the Appointments Clause because, under the standard articulated by this Court in *Freytag v. Commissioner of Internal Revenue*, 501 U.S. 868 (1991), they exercise "significant authority" over SEC administrative enforcement proceedings. *See Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016), *petition for cert. filed* (U.S. Sept. 29, 2017) (No. 17-475); *Ironridge Glob. IV, Ltd. v. SEC*, 146 F. Supp. 3d 1294 (N.D. Ga. 2015), *appeal dismissed*, No. 16-10205 (11th Cir. Sept. 27, 2016); *Duka v. SEC*, 103 F. Supp. 3d 382 (S.D.N.Y 2015), *vacated on other grounds*, No. 15-2732 (2d Cir. June 13,

2016); *Gray Fin. Grp., Inc. v. SEC*, 166 F. Supp. 3d 1335 (N.D. Ga. 2015), *vacated on other grounds sub nom. Hill v. SEC*, 825 F.3d 1236 (11th Cir. 2016); *Hill v. SEC*, 114 F. Supp. 3d 1297, 1316-19 (N.D. Ga. 2015), *rev'd on other grounds*, 825 F.3d 1236 (11th Cir. 2016); *cf. Burgess v. FDIC*, 871 F.3d 297, 299-301 (5th Cir. 2017) (staying order by Federal Deposit Insurance Corporation ("FDIC") based on finding that appellant was likely to succeed on his claim that the FDIC ALJ who presided over his proceeding was an "inferior Officer" subject to—but not appointed consistently with—the Appointments Clause).

The RDLC *Amici* respectfully submit that a "case study" of their experience over the last nineteen months vividly illustrates the significant authority that SEC ALJs wield over every phase and facet of an administrative enforcement proceeding. This control is not limited to the power to issue what may become a final order imposing significant penalties at the conclusion of the hearing, but also includes the authority to make decisions at every stage of the administrative hearing process that, as a practical matter, can have a profound impact on the development of the record and the ultimate outcome of the proceeding.

A. The SEC ALJ Exercised Significant Authority over Important Prehearing Issues in the RDLC *Amici*'s Administrative Proceeding

Following a nearly two-year investigation, the Commission initiated an administrative proceeding against the RDLC *Amici* by filing an OIP on July 14, 2016. *See In the Matter of RD Legal Capital, LLC and Roni Dersovitz*, Administrative Proceeding File No. 3-17342 (July 14, 2016). The OIP asserts complicated

securities fraud claims and seeks tens of millions of dollars in damages against the RDLC *Amici*, as well as the imposition of a lifetime industry bar, which has been called the "securities industry equivalent of capital punishment." *PAZ Sec., Inc. v. SEC*, 494 F.3d 1059, 1065 (D.C. Cir. 2007). The Commission, however, elected not to prosecute its claims in federal court, where the RDLC *Amici* would have the due process protections of the Federal Rules of Civil Procedure and the Federal Rules of Evidence, broad discovery rights, and the opportunity to present their defenses to a jury. Instead, the Commission decided to give itself a literal "home court" advantage by bringing an administrative enforcement proceeding before an SEC ALJ.

The Commission's decision to have its claims against the RDLC *Amici* heard by an SEC ALJ rather than an Article III judge is not surprising. "The SEC won against 90% of defendants before its own judges in cases from October 2010 through March [2015]," which is "markedly higher than the 69% success rate the agency obtained against defendants in federal court over the same period." Jean Eaglesham, *SEC Wins with In-House Judges*, Wall St. J., May 6, 2015. The Commission accordingly has a powerful incentive to keep claims—particularly marginal claims such as those it asserted against the RDLC *Amici*—out of federal court, where they may not survive even the pleadings stage, and instead litigate those claims in a more favorable and forgiving forum. *Cf. SEC v. Mapp*, 240 F. Supp. 3d 569, 593 (E.D. Tex. 2017) (dismissing SEC enforcement action for a second time on the pleadings, with prejudice, based on conclusion that "[a]s alleged, [defendant's] conduct simply does not give rise to liability under the federal securities laws as they exist today

[, a]nd it is not the province of the Court to stretch federal securities laws beyond their scope to prescribe liability based on moral considerations or policy concerns").

One of the reasons the Commission's "home court" advantage in administrative enforcement proceedings is so strong is that its ALJs wield significant authority regarding virtually every aspect of the proceedings over which they preside, including at the prehearing stage. As explained below, rulings made—or refused to be made—by the SEC ALJ at the prehearing stage of the case against the RDLC *Amici* had a major impact on the ability of the RDLC *Amici* to prepare their defenses and, later, to present those defenses in order to have meritless claims dismissed.

1. The SEC ALJ Declined to Require That the OIP Provide Sufficient Notice of the Commission's Fraud Claims

Because the Federal Rules of Civil Procedure do not apply in SEC enforcement proceedings, the Division of Enforcement was not required to plead its fraud claims with particularity as required by Rule 9 of the Federal Rules of Civil Procedure. Faced with an OIP that lacked the particularity necessary for the RDLC *Amici* to adequately prepare their defenses, the RDLC *Amici* invoked the only procedural mechanism available under the SEC's Rules of Practice, and filed a Motion for a More Definite Statement. *See* 17 C.F.R. § 201.220(d) (Rule 220(d)). The SEC ALJ, however, simply declined to rule on the motion, forcing the RDLC *Amici* to defend themselves against fraud charges without notice of the "who, what, where, or when" of the Commission's fraud allegations.

2. The SEC ALJ Issued Discovery Rulings That Impeded Preparation of the RDLC *Amici*'s Defenses

In addition to declining to rule on a motion to clarify the pleadings, the SEC ALJ further prevented the RDLC *Amici* from preparing their defense against the Commission's case by issuing several rulings that curtailed the RDLC *Amici*'s access to discovery.

The Commission filed the OIP following a prolonged investigation, during which the RDLC *Amici* cooperated fully with the Division of Enforcement, producing approximately one million pages of documents. In conducting its investigation, the Commission also: (a) obtained testimony from five of RDLC's employees, as well as from certain third parties, including the independent valuation firm for the Funds; (b) had the ability to take unlimited *ex parte* testimony of witnesses, backed by national subpoena power; (c) received approximately one million pages of additional documents in response to third-party subpoenas; and (d) contacted and interviewed dozens of investors. The Commission had three Division of Enforcement staff attorneys working on the matter consistently throughout the investigation, and up to five staff members attending the testimony in the case—sometimes double- or triple-teaming witnesses during questioning without defense counsel present.

In contrast to the extensive investigative powers available to—and exercised by—the Commission, the RDLC *Amici*'s access to and time for discovery was significantly limited by the SEC ALJ's rulings. The SEC ALJ set a discovery, motion, and hearing schedule

that required hearing preparation—including review of more than two million pages—on an expedited basis. *See RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 4237 (ALJ Oct. 7, 2016). The hearing—initially set for a mere month after the OIP was issued—was continued for only seven months for the RDLC *Amici* to review and analyze the Commission's massive document production, conduct their own discovery, and prepare their defense. *See RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 3988 (ALJ July 15, 2016); *RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 4086 (ALJ Aug. 23, 2016).

In addition to the voluminous number of documents it collected during the investigation, the Division of Enforcement sought and obtained leave from the SEC ALJ to issue additional document subpoenas to RDLC and others during the administrative proceeding—which the SEC ALJ herself acknowledged was "unusual." *See RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 4387 (ALJ Nov. 23, 2016). Moreover, during the prehearing process, the Division of Enforcement served an initial witness list that identified more than fifty witnesses—many of whom appeared to have no connection to the case. Under 17 C.F.R. § 201.233(a)(2) (Rule 233(a)(2)), the RDLC *Amici* (with permission from the SEC ALJ) were permitted to depose just *five* witnesses collectively.[3] The RDLC *Amici*

3. The allowance of five depositions was the result of the 2016 amendments to the SEC's Rules of Practice, which, by agreement of the parties, apply to the administrative proceeding for the RDLC *Amici*. *See RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 4036 (ALJ Aug. 2, 2016).

felt compelled to devote some of their five depositions to depose certain of these "mystery" witnesses in order to determine the substance of their testimony, only to find that most of those witnesses were not included in the Division of Enforcement's final witness list. And when the RDLC *Amici* requested that the SEC ALJ grant them leave to take the maximum number of two additional depositions allowed under 17 C.F.R. § 201.233(a)(3) (Rule 233(a)(3)), the SEC ALJ initially granted leave for the depositions, *see RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 4499 (ALJ Jan. 4, 2017), only to later quash two of the deposition subpoenas—including one to a key witness because of the witness's vacation schedule. *See RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 4526 (ALJ Jan. 13, 2017).

3. The SEC ALJ Declined to Permit a Dispositive Motion by the RDLC *Amici* before Being Replaced on the Eve of the Hearing

The SEC ALJ also prevented the RDLC *Amici* from narrowing the issues prior to the hearing. On the evening that discovery closed—*i.e.*, the very first opportunity for filing a dispositive motion based on lack of evidence—the RDLC *Amici* filed a request to bring a dispositive motion on the ground that the Commission had no evidentiary support for one of its two theories of liability (*i.e.*, that the RDLC *Amici* had improperly valued the assets in the portfolios of the Funds they manage). So that the motion could be heard before the administrative hearing commenced under the expedited scheduling order the SEC ALJ had issued, the RDLC *Amici* agreed to waive their

right to submit a reply brief. The SEC ALJ nonetheless determined that the motion was untimely. *See RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 4622 (ALJ Feb. 23, 2017) at 1 ("The request [for leave to file a motion for summary disposition] will be denied as untimely.").

The SEC ALJ's refusal to entertain the RDLC *Amici*'s dispositive motion—despite the fact that it was filed on the very day discovery closed—denied the RDLC *Amici* the opportunity to streamline the case against them, and forced them to devote substantial time and resources before and during the hearing to defend against a claim that was wholly lacking in merit or evidentiary support. The SEC ALJ's refusal to entertain a motion to dismiss the Commission's baseless valuation claim prior to the hearing was devastating to the RDLC *Amici*'s business, as the public allegation that the company was cooking its books was damning to the RDLC *Amici*'s reputations, and the SEC ALJ prevented the RDLC *Amici* from clearing their names from the Commission's meritless smears.

In a remarkable twist, on March 9, 2017—one day after the RDLC *Amici* filed their prehearing briefs and less than two weeks before the start of the administrative proceeding—the Commission, without any explanation, assigned a new SEC ALJ to preside over the administrative hearing. *See RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 4670 (ALJ Mar. 9, 2017). The RDLC *Amici* asked the newly appointed SEC ALJ to entertain a dispositive motion on the valuation issue following the close of evidence at the administrative hearing. After initially denying the motion, the SEC ALJ issued an order on August 16, 2017 granting

summary dismissal of the Commission's valuation claims and confirming that the "valuation allegations are unfounded. . . ." *RD Legal Capital, LLC*, SEC Admin. Proc. File No. 3-17342, Rulings Release No. 4976 (ALJ Aug. 16, 2017) at 1; *see also id.* at 15 ("Having carefully scrutinized the Division's recitation of all evidence on this issue, I find that, as a matter of law, its allegations on valuation amount to nothing.").

The dramatic reversal in the fortunes of the Commission's damaging yet meritless valuation claim following the assignment of a new SEC ALJ highlights the significant discretion and authority that individual SEC ALJs exercise in the administrative enforcement proceedings over which they preside. Moreover, as the RDLC *Amici*'s case illustrates, an SEC ALJ's exercise of its discretion and authority can have severe economic and practical consequences for litigants forced to defend themselves in those proceedings.

B. The SEC ALJ Exercised Significant Authority During the RDLC *Amici*'s Five-Week Administrative Hearing

The administrative hearing against the RDLC *Amici* was held from March 20, 2017 through April 27, 2017. It was presided over by an SEC ALJ in a courtroom at the United States District Court for the Eastern District of New York. Forty-three witnesses testified during the trial, and the transcript spans 7,214 pages. The ALJ admitted 1,059 exhibits into evidence. To any of the dozens of witnesses who testified, to the reporters who covered the hearing, and to the spectators who attended, as well as to the parties and their counsel, there was no question that the SEC ALJ, sitting on the bench in a black robe, controlling the

proceeding, and making dozens of rulings on a daily basis, was exercising significant governmental authority.

The SEC ALJ made countless rulings during the proceeding, including on, among other things: the propriety of questioning; the admissibility of each exhibit; the competency of witnesses (including a *Daubert* challenge by the RDLC *Amici* that was granted, in part); the ramifications of alleged *Brady* and *Jencks* violations; the production of additional documents; and dozens of administrative issues. The SEC ALJ also administered oaths to every witness, questioned certain witnesses himself, directed counsel to question witnesses about certain topics, and generally controlled the course of the hearing. In addition, the SEC ALJ ruled on many motions brought by both parties—including the Division of Enforcement's motions to preclude certain affirmative defenses or find a waiver of the attorney-client privilege, multiple motions for a directed verdict in favor of the RDLC *Amici* (one of which was ultimately granted), and the RDLC *Amici*'s motions to dismiss the proceeding on several constitutional grounds, including based on violations of the Appointments Clause.

Following the proceeding, the parties filed multiple post-trial briefs, and the Division of Enforcement submitted 406 pages of proposed findings of fact, requiring the SEC ALJ to make factual and credibility determinations on 741 individual proposed facts and hundreds of sub-facts.

The importance of the SEC ALJ's gatekeeping role in compiling such a massive administrative record and preparing an Initial Decision is indisputably significant. As a practical matter, there is no way the Commission—in

the event it is called upon to review the forthcoming Initial Decision—could review *all of the evidence* submitted in the RDLC *Amici*'s five-week trial without the filter and gloss of the ALJ's Initial Decision, and it certainly could not make the important credibility determinations that the SEC ALJ presiding over the administrative proceeding is uniquely positioned to make. Indeed, during the course of the *Lucia* case, the Commission even acknowledged that an SEC ALJ's determination has "considerable importance," because the ALJ is "in the best position to make findings of fact, including credibility determinations, and resolve any conflicts in the evidence." Pet. App. 241a; *see also* Brief for Petitioners ("Pet'rs Brief"), at 24; Brief for Respondent Supporting Petitioners ("Top-Side Brief"), at 24; *In re Clawson*, Exchange Act Release No. 48,143, 2003 WL 21539920, at *2 (July 9, 2003) ("We accept [an SEC ALJ's] credibility finding, absent *overwhelming evidence* to the contrary.") (emphasis added). Thus, if there was any doubt about the authority afforded to an SEC ALJ in an administrative proceeding, the SEC ALJ's responsibility to compile an administrative record, analyze the reams of evidence submitted by both parties, and eventually issue an Initial Decision that will receive deference if subject to review, confirms that SEC ALJs exercise significant authority.[4]

4. In contrast, if SEC ALJs were truly SEC "employees" who lack independent discretion but preside over administrative proceedings anyway—as the Commission previously asserted—then the Commission is acting through its agents as both prosecutor and judge, adding to the significant due process problems that already plague SEC administrative proceedings. *See Williams v. Pennsylvania*, 136 S. Ct. 1899, 1905 (2016) ("[A]n unconstitutional potential for bias exists when the same person serves as both accuser and adjudicator in a case.").

II. THE COMMISSION'S RATIFICATION ORDER PERPETUATES ITS FLOUTING OF THE APPOINTMENTS CLAUSE

On November 30, 2017—one day after the Solicitor General admitted in a brief filed on the Commission's behalf that SEC ALJs exercise significant authority and thus are executive officers under the Appointments Clause—the Commission issued the Ratification Order, which sought "[t]o put to rest any claim that administrative proceedings pending before, or presided over by, Commission administrative law judges violate the Appointments Clause." *See* Order, *In re Pending Administrative Proceedings*, Securities Act Release No. 10,440, 2017 WL 5969234, at *1 (Nov. 30, 2017).

The Ratification Order employs two separate "ratification" strategies to achieve its objective. First, the Ratification Order states that "the Commission—in its capacity as head of a department—hereby ratifies the agency's prior appointment of Chief Administrative Law Judge Brenda Murray and Administrative Law Judges Carol Fox Foelak, Cameron Elliot, James E. Grimes, and Jason S. Patil." *Id.* Second, the Ratification Order requires all SEC ALJs presiding over pending matters to "[r]econsider the record" and to "[d]etermine, based on such reconsideration, whether to ratify or revise in any respect all prior actions taken by an administrative law judge in the proceeding . . . ." *Id.* at 1-2.

As explained below, however, *neither* of these two components of the Ratification Order can cure the constitutional defects in SEC administrative enforcement proceedings. The Ratification Order does not and

cannot change the fact that the Commission violated the Appointments Clause when it forced the RDLC *Amici* and other respondents to participate in administrative enforcement proceedings presided over by individuals who had not been appointed by the Commission. Those violations warrant dismissal of *all* administrative enforcement proceedings conducted before an unconstitutional SEC ALJ, as the Commission cannot cure through ratification structural defects in the constitutionality of those proceedings. *See Edmond v. United States*, 520 U.S. 651, 659 (1997) ("[T]he Appointments Clause of Article II is more than a matter of 'etiquette or protocol'; it is among the significant structural safeguards of the constitutional scheme.") (citing *Buckley v. Valeo*, 424 U.S. 1, 125 (1976) (per curiam)).[5]

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5. In addition to failing to cure the Appointments Clause violations, the Ratification Order does not address, let alone attempt to remedy, the separation-of-powers infirmity caused by the multiple layers of tenure protection afforded to SEC ALJs. As this Court held in *Free Enterprise Fund v. PCAOB*, 561 U.S. 477, 492 (2010), Article II requires that executive officers not be protected from removal by their superiors at will when those superiors are themselves protected from removal by the President at will. *See also id.* at 483-84 (holding that "multilevel protection from removal is contrary to Article II's vesting of the executive power in the President"). SEC ALJs, however, enjoy multiple layers of protection from removal, which—as in *Free Enterprise Fund*—impairs the President's ability to ensure that the laws are faithfully executed. *See id.* at 498. Because the President cannot oversee SEC ALJs in accordance with Article II, administrative proceedings presided over by those judges violate separation-of-powers principles embedded in the Constitution. *See* Top-Side Brief, at 39-45.

A. The Commission Cannot Ratify Prior "Appointments" of Its SEC ALJs

The Commission's attempt to retroactively "ratif[y] the agency's prior appointment" of its SEC ALJs is ineffective because *there were no prior appointments to ratify*. As the Commission concedes, it abdicated its constitutional obligation to appoint SEC ALJs in favor of a hiring process that delegated to the Chief SEC ALJ and the Commission's Office of Human Resources the task of vetting and selecting SEC ALJs. The Commission cannot use the ratification doctrine to rewrite history and magically transform an unconstitutional delegation of hiring authority into a "prior appointment." Indeed, the Commission's attempted ratification perpetuates, rather than cures, its Appointments Clause violations because the ratification doctrine, by its nature, presupposes the ability of a principal to delegate authority to an agent, and the delegation of appointment authority is the very thing that the Appointments Clause prohibits.

1. Ratification Cannot Convert a Hiring into an Appointment

The Commission's attempt to cure the Appointments Clause violations by "ratif[ying] the agency's prior appointment" of SEC ALJs must fail because, as the Commission itself has conceded, none of the SEC ALJs were ever "appointed" by the agency. The ALJs currently employed by the Commission instead were vetted through a competitive examination process conducted by the Office of Personnel Management, and ultimately were selected not by the Commission, but by the Chief SEC ALJ, "subject to approval by the Commission's Office of

Human Resources on the exercise of authority *delegated* by the Commission." Top-Side Brief at 3 (emphasis added); *see also id.* at 38.

This accordingly is not a situation where the Commission sought in good faith to appoint SEC ALJs in a manner consistent with the Appointments Clause but made some mistake that rendered the appointments constitutionally defective. To the contrary, prior to its recent conversion, the Commission long eschewed any obligation to appoint SEC ALJs, and instead argued vehemently for years that SEC ALJs were "employees" who were not, and did not need to be, appointed in accordance with the Appointments Clause. *See, e.g., Bandimere*, 844 F.3d at 1176 (acknowledging the Commission's concession that SEC ALJs "are not appointed" in conformity with the Appointments Clause). Thus, despite how it is described in the Ratification Order, the Commission's effort to retroactively convert a constitutionally infirm delegation of hiring authority into a constitutionally permissible appointment process would not be a *ratification* of the Commission's prior acts, but rather a *mischaracterization* of those acts. A ratification can confirm that an apple is an apple, but it cannot transform an apple into an orange. Or, put another way, the Ratification Order cannot ratify something that *did not happen*.

2. The Ratification Doctrine Has No Relevance Here

The ratification doctrine arises out of principles of agency law. *See FEC v. NRA Political Victory Fund*, 513 U.S. 88, 98 (1994) (analyzing whether Solicitor General could retroactively authorize filing of certiorari petition,

and noting that "[t]he question is at least presumptively governed by principles of agency law, and in particular the doctrine of ratification"). "Ratification is the affirmance of a prior act done by another, whereby the act is given effect *as if done by an agent acting with actual authority.*" Restatement (Third) of Agency § 4.01 (2006) (emphasis added); *see also GDG Acquisitions LLC v. Gov't of Belize*, 849 F.3d 1299, 1310 (11th Cir. 2017) ("[T]he doctrine of ratification starts with the assumption that the agent did not have actual authority at the time he acted.").

The ratification doctrine thus *presupposes* that a principal has the power to authorize an agent to act on its behalf, and is designed to address situations where the agent did not have such authorization from the principal at the time the agent acted. *See Marsh v. Fulton Cty.*, 77 U.S. (10 Wall.) 676, 684 (1870) (ratification "operates upon the act ratified in the same manner as though the authority of the agent to do the act existed originally"). As one court described:

> Ratification results when a principal affirms a previous unauthorized act by his agent. The effect of ratification is to give the principal's agent the authority to perform the unauthorized act as of the time the agent performed the unauthorized act. In essence, ratification by a principal of his agent's unauthorized act is equivalent to the agent having that particular authority from the beginning.

In re Packer Ave. Assocs. v. Johnstone, 1 B.R. 286, 292 (Bankr. E.D. Pa. 1979) (citation omitted); *see also GDG Acquisitions*, 849 F.3d at 1310 ("It is precisely on account

of the principal's subsequent consent that the prior unauthorized act 'is given effect as if done by an agent acting with actual authority.'") (quoting Restatement (Third) of Agency § 4.01(1)).

Here, however, the Appointments Clause violations were not the result of the Chief SEC ALJ hiring SEC ALJs without "actual authority" from the Commission. To the contrary, the undisputed facts leave no doubt that the Commission affirmatively sought to delegate[6] to the Chief SEC ALJ the authority to hire SEC ALJs, and thus, from an agency law perspective, the Chief SEC ALJ had "actual authority" to make those hiring decisions on behalf of the Commission. *See* Restatement (Third) of Agency § 2.01 (2006) ("An agent acts with actual authority when, at the time of taking action that has legal consequences for the principal, *the agent reasonably believes, in accordance with the principal's manifestations to the agent, that the principal wishes the agent so to act.*") (emphasis added).

Instead, the Appointments Clause places constitutional limits on the *Commission's* ability to delegate to an agent authority to act on the Commission's behalf when it comes to appointing "Officers of the United States" such as SEC ALJs, and it was the *act of delegation*, not the *absence of actual authority*, that caused the constitutional violations. The ratification doctrine the Commission purports to rely on to cure its Appointments Clause violations accordingly has no relevance here, and cannot be used to permit

6. While the Commission has taken the position that it delegated its appointment power to the Chief SEC ALJ, it is not clear that it followed the proper procedure to do so. *See* 15 U.S.C. 78d-1(a) (requiring the Commission to delegate its functions only "by published order or rule").

the Commission to accomplish, *mutatis mutandis*, the delegation of authority that the Appointments Clause expressly prohibits. *See District Twp. of Doon v. Cummins*, 142 U.S. 366, 376 (1892) ("[A] ratification can have no greater effect than a previous authority."); *see also* Cal. Civ. Code § 2312 (West 2018) ("A ratification is not valid unless, at the time of ratifying the act done, the principal has power to confer authority [to an agent] for such an act."); *Stowe v. Maxey*, 84 Cal. App. 532 (Cal. Ct. App. 1927) (holding board of supervisors having no authority to delegate power to corporation to hold county fair could not ratify corporation's action thereunder).

3. The Ratification Order Itself Violates the Appointments Clause

The Commission can *never* confer upon its Chief SEC ALJ—whether in the first instance or through ratification—the authority to appoint other SEC ALJs. That appointment power is conferred by the Appointments Clause exclusively to the commissioners themselves, as the head of a department under the Constitution. *See* U.S. Const. Art. II, § 2, cl. 2 (dictating that inferior officers must be appointed by the President, the head of a department, or a court of law); *Free Enter. Fund*, 561 U.S. at 512-13 (commissioners are the "head of a department" for purposes of Appointments Clause); *Buckley*, 424 U.S. at 118 (holding that the Appointments Clause establishes the "*exclusive method* by which those charged with executing the laws of the United States may be chosen") (emphasis added).

Because its prior delegation of hiring authority is the very thing that the Appointments Clause prohibits, the Commission does not have the power to ratify such improper delegation retroactively. This Court has recognized that "it is *essential* that the party ratifying should be able . . . *to do the act ratified*," both "at the time the act was done" and "*at the time the ratification was made*." *NRA Political Victory Fund*, 513 U.S. at 98 (first two emphases added) (quoting *Cook v. Tullis*, 85 U.S. (18 Wall.) 332, 338 (1874)). In *NRA Political Victory Fund*, the Court rejected the Solicitor General's attempt to ratify the filing of a *certiorari* petition by the Federal Election Commission on the ground that the Solicitor General itself lacked authority at the time of its purported ratification to do the act that it sought to ratify. *See* 513 U.S. at 98 ("Here, the Solicitor General attempted to ratify the FEC's filing on May 26, 1994, but he could not himself have filed a petition for certiorari on that date because the 90-day time period for filing a petition had expired on January 20, 1994. His authorization simply came too late in the day to be effective.").

As in *NRA Political Victory Fund*, the Commission here itself lacks the authority to do the act it seeks to ratify—*i.e.*, delegation of the selection and hiring of SEC ALJs to others. The Commission's attempt in the Ratification Order to accomplish through retroactive "ratification" that which it lacks the constitutional authority to do in the first place accordingly must be rejected. *See Newman v. Schiff*, 778 F.2d 460, 467 (8th Cir. 1985) ("Ratification serves to authorize that which was unauthorized. Ratification cannot, however, give legal significance to an act which was a nullity from the start."). Indeed, by reaffirming through the Ratification Order its prior authorization of the Chief SEC ALJ's

prior acts, the Commission persists in flouting its constitutional obligations, and compounds rather than cures its Appointments Clause violations. *See* Order, *In re Pending Administrative Proceedings*, Securities Act Release No. 10,440, 2017 WL 5969234, at *1 (Nov. 30, 2017) (purporting to ratify the "agency's prior appointment" of SEC ALJs). This Court accordingly should find that the Ratification Order itself violates the Appointments Clause, and that the RDLC *Amici* and all other respondents in pending administrative proceedings are entitled to new proceedings before constitutionally appointed officers.

4. The RDLC *Amici* Are Unaware of Any Instance in Which an Appointments Clause Violation Has Been Cured Through Ratification

In a brief filed in the administrative proceeding against the RDLC *Amici*, the Commission's Division of Enforcement cited several cases that it claimed support the Commission's ability to cure any Appointments Clause violations by ratifying the Chief SEC ALJ's prior hiring decisions. *See CFPB v. Gordon*, 819 F.3d 1179 (9th Cir. 2016); *Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd.*, 796 F.3d 111 (D.C. Cir. 2015); *Doolin Sec. Sav. Bank, F.S.B. v. Office of Thrift Supervision*, 139 F.3d 203 (D.C. Cir. 1998); *FEC v. Legi-Tech*, 75 F.3d 704 (D.C. Cir. 1996). In each of these cases, however, the Appointments Clause violation was cured not through a retroactive ratification of a *defective prior* "appointment" (as the Commission improperly attempts to do in its Ratification Order), but rather through a two-step process in which a *valid subsequent* appointment permitted the now properly appointed officer to ratify prior unauthorized acts.

In *CFPB v. Gordon*, for example, Director Richard Cordray was not able to ratify his prior unauthorized acts as Director of the Consumer Finance Protection Bureau until he was subsequently confirmed by the Senate. 819 F.3d at 1185-86; *see id.* at 1190–91 ("The initial invalid appointment of Cordray also is not fatal to this case. The *subsequent valid appointment*, coupled with Cordray's August 30, 2013 ratification, cures any initial Article II deficiencies.") (emphasis added). Notably, the Senate did not seek to ratify Director Cordray's previous improper recess appointment—the equivalent of what the Commission is attempting to do with its Ratification Order. The Senate instead undertook a constitutional appointment process, and Director Cordray, once properly appointed, was then able to ratify his prior unauthorized acts. The Appointments Clause dictated that there be a constitutionally sound appointment prior to Director Cordray ratifying his otherwise unauthorized acts. *See Buckley*, 424 U.S. at 125.

Similarly, each of the three D.C. Circuit ratification cases the Division of Enforcement relied on involved ratification of prior acts *following* a subsequent valid appointment, *not* the ratification of a prior hiring or "appointment" that was made in violation of the Appointments Clause. *See Intercollegiate Broad.*, 796 F.3d at 117 ("Intercollegiate does not dispute that the three new Judges were properly appointed by the Librarian under the Appointments Clause."); *Doolin*, 139 F.3d at 213-14 (D.C. Cir. 1998) (holding that a *validly appointed agency director* had "made a detached and considered judgment" in ratifying the previous director's decision); *FEC v. Legi-Tech*, 75 F.3d at 706 (holding that a *properly reconstituted* Federal Election Commission could reauthorize pending

enforcement actions that had been initiated by an unconstitutionally constituted Commission).

These cases, even if properly decided, accordingly provide no support for the Commission's improper effort to retroactively ratify a selection and hiring process for SEC ALJs that even the Commission now concedes violated the Appointments Clause, and the RDLC *Amici* are unaware of any case holding that an Appointments Clause violation can be cured through ratification in the absence of a subsequent valid appointment. This lack of supporting precedent for the Commission's position makes sense given that—as explained above—ratification is an agency law doctrine that permits a principal to confirm that it has delegated to its agent the authority to act, but has no bearing on whether the principal has the constitutional authority to make such a delegation in the first place. As it relates to the appointment of "Officers of the United States," this second question is answered by the Appointments Clause itself, and the answer is no.

B. SEC ALJs Cannot Ratify Prior Denials of Appointments Clause Challenges

The Commission's instruction in the Ratification Order requiring SEC ALJs to "[r]econsider the record" and to "[d]etermine . . . whether to ratify or revise in any respect all prior actions" likewise does not cure its Appointments Clause violations. As a threshold matter, for all of the reasons articulated in Petitioners' Brief, a citizen subjected to proceedings before an unconstitutionally appointed adjudicator is entitled to entirely new proceedings before an executive officer appointed in conformity with the Appointments Clause. *See* Pet'rs Brief

at 43-49. Moreover, while the Commission undeniably has the authority to appoint individuals to serve as SEC ALJs, the Commission has not exercised that authority—in the Ratification Order or elsewhere—to appoint the current SEC ALJs. And even if the Commission were to appoint the current SEC ALJs and could simply order them to revisit their prior rulings—a procedure that has never been endorsed by this Court—those SEC ALJs would have no choice but to *reverse* their prior denials of Appointments Clause challenges because, as the Commission itself now concedes, the SEC ALJs had not been properly appointed at the time that those challenges were brought, and those challenges accordingly were—and continue to be—meritorious.

1. The Ratification Order Fails to Appoint the SEC ALJs in the Manner Required by the Appointments Clause

The RDLC *Amici* recognize that the Commission has authority as the "head of a department" to appoint SEC ALJs in conformity with the Appointments Clause. *Free Enter. Fund*, 561 U.S. at 512-13 (commissioners are the "head of a department" for purposes of Appointments Clause). The Commission, however, has not yet exercised that authority. As discussed above, the Ratification Order instead improperly attempts to ratify a prior act that violated the Appointments Clause. While the Ratification Order goes on to instruct SEC ALJs to "[r]econsider" and "ratify or revise" all prior actions, it *fails to appoint* the SEC ALJs in the manner required by the Appointments Clause, and thus never imbues the SEC ALJs with the authority necessary to engage in that process. Moreover, as explained below, even if the Commission

were to subsequently exercise its authority to appoint the SEC ALJs, prior motions to dismiss administrative proceedings—such as the ones repeatedly filed by the RDLC *Amici*—should have been granted.

2. Even Properly Appointed SEC ALJs Could Not Ratify Prior Denials of Appointments Clause Challenges

This Court has never endorsed the ratification of adjudicative acts by an unconstitutionally appointed adjudicator, but the D.C. Circuit has held that a properly appointed official can revisit and ratify prior adjudicative acts taken by an improperly appointed official. *Compare Ryder v. United States*, 515 U.S. 177, 188 (1995) (reversing judgment by Coast Guard Court of Military Review based on Appointments Clause violation and holding that "[p]etitioner is entitled to a hearing before a properly appointed panel of that court") *with Intercollegiate Broad.*, 796 F.3d at 117-18 (allowing ratification of decision of unconstitutionally constituted Copyright Royalty Board). Even if *Intercollegiate* were correctly decided, however—a point that is far from clear under *Ryder* and this Court's Appointments Clause jurisprudence—the "ratifier" cannot just "blindly affirm the earlier decision without due consideration," but instead "must make a detached and considered affirmation of the earlier decision." *Advanced Disposal Servs. E., Inc. v. NLRB*, 820 F.3d 592, 602-03 (3d Cir. 2016); *see also Wilkes-Barre Hosp. Co., LLC v. NLRB*, 857 F.3d 364, 371 (D.C. Cir. 2017) ("Our precedents establish that ratification can remedy a defect arising from the decision of 'an improperly appointed official . . . when . . . a properly appointed official *has the power to conduct an independent evaluation*

of the merits and does so.'") (emphasis added) (quoting *Intercollegiate Broad.*, 796 F.3d at 117-21, 124).

Here, an independent reevaluation of the merits of prior constitutional challenges brought by the RDLC *Amici* and other respondents would require dismissal of the tainted proceedings. In the administrative proceeding for the RDLC *Amici*, for example, each time the SEC ALJ rejected the Appointments Clause challenges, he did so solely on the ground that he lacked authority to contravene the Commission's prior (erroneous) determination that SEC ALJs were not "inferior officers" subject to the Appointments Clause. Now, however, the Commission has reversed its position, and agrees that the RDLC *Amici*'s administrative proceeding was presided over by an "inferior officer" who was not appointed in conformity with the Appointments Clause. Thus, in the absence of an impermissible "blind affirmance," there is no way for the SEC ALJ to conclude that the RDLC *Amici*'s motions to dismiss based on Appointments Clause violations should not have been granted at the time they were brought.

This Court has recognized that proceedings before an improperly appointed judge must be set aside. *See, e.g.*, *Ryder*, 515 U.S. at 188 (holding Appointments Clause violation "entitled [petitioner] to a hearing before a properly appointed" court); *Nguyen v. United States*, 539 U.S. 69, 77-83 (2003) (rejecting the "*de facto* officer" doctrine and vacating judgments based on determination that a Ninth Circuit panel consisting of two Article III judges and one Article IV judge lacked authority to decide the appeals); *see also Bandimere*, 844 F.3d at 1172, 1188 (setting aside Commission's opinion based on Appointments Clause violation and

recognizing that resolving the Appointments Clause challenge in petitioner's favor "relieves Mr. Bandimere of all liability"). SEC administrative enforcement actions where a citizen's assets and very livelihood are at stake are exactly the type of proceedings that involve the exercise of significant governmental authority, and those proceedings accordingly *must* be set aside if they are not presided over by a duly appointed officer. Actions taken by an SEC ALJ who has not been appointed in accordance with the Appointments Clause accordingly are *void ab initio*, and cannot be transmogrified into official acts by later ratification.

****

"Ratification" is not a magical incantation that can be wielded indiscriminately to transform what the Commission now concedes was a constitutionally improper hiring process into a proper exercise of the Commission's authority under the Appointments Clause. And any *subsequent* valid appointment would not change the fact that, at the time the RDLC *Amici* challenged the constitutionality of their administrative proceeding, the SEC ALJs presiding over the proceeding had not been appointed in the manner required by the Appointments Clause, and the motions to dismiss the unconstitutional proceeding therefore *should have been granted.*

CONCLUSION

The Commission was well aware at the time that it issued its OIP against the RDLC *Amici* of the multiple pending challenges to the constitutionality of its administrative enforcement proceedings, including

challenges based on the Appointments Clause. Instead of filing its case in federal court and avoiding those issues, however, the Commission commenced an administrative proceeding against the RDLC *Amici*, fought the RDLC *Amici*'s constitutional challenges in multiple venues, and assumed the risk that the Appointments Clause issue would ultimately be decided against the Commission. Having assumed that risk and subjected the RDLC *Amici* and other citizens to prolonged proceedings that lacked the constitutional safeguards mandated by Article II, the Commission cannot wipe away its own constitutional violations with a simple stroke of the pen. Our Constitution demands more. *See Edmond v. United States*, 520 U.S. 651, 659 (1997) ("[T]he Appointments Clause of Article II is more than a matter of 'etiquette or protocol'; it is among the significant structural safeguards of the constitutional scheme.") (citing *Buckley*, 424 U.S. at 125).

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No. 17-130

In The
Supreme Court of the United States

RAYMOND J. LUCIA, *ET AL.*,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

AMICUS CURIAE BRIEF OF ANTHONY MICHAEL SABINO IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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INTEREST OF *AMICUS CURIAE*

This *amicus curiae* is a law professor with expertise in constitutional law, securities regulation, and securities litigation. Furthermore, this *amicus curiae* has represented parties in proceedings before the Securities and Exchange Commission (the "SEC" or the "Commission"), and regularly lectures on the precise topics found in the pending controversy. This case addresses the interpretation of the Appointments Clause of Article II of the Constitution, and implicates the proper conduct of enforcement proceedings before the SEC. This *amicus curiae* has a professional and scholarly interest in the proper application and development of the law in these domains.[1]

STATEMENT

This *amicus curiae* respectfully adopts, in relevant part, the Statement of Facts set forth by the Petitioners herein, Raymond J. Lucia., *et al.* ("Petitioners").

[1] No counsel for a party authored this brief in whole or in part, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. Counsel of record received timely notice of the intent to file this brief, as required by Supreme Court Rule 37.3(a). Petitioners, Respondent, and counsel appointed to defend the decision below all consented to this filing.

SUMMARY OF ARGUMENT

The Court's decision herein shall clarify the appropriate methodology for the constitutional appointment of ALJs across a wide range of administrative agencies, thereby cabining executive power, reinforce the Court's recent landmarks interpreting the Appointments Clause of Article II, resolve the internecine conflict among the circuit courts of appeals as to the constitutionality of the present mode of appointing SEC Administrative Law Judges ("ALJs"), and, above all else, uphold axioms of checks and balances and the separation of powers, in particular Article II's structural constraints upon the exercise of executive power.

ARGUMENT

I. THE COURT'S DECISION SHALL CLARIFY THE CONSTITUTIONALITY OF THE APPOINTMENT PROCESS FOR ALL ALJs ACROSS A WIDE RANGE OF ADMINISTRATIVE BODIES, THEREBY CABINING EXECUTIVE POWER.

While the question presented is limited to the constitutionality of the appointment of SEC ALJs, the edict to be issued by the Court shall have decisive ramifications for the appointment of all administrative adjudicators and their respective agencies. Moreover, the Court's decision shall appropriately cabin executive power, consistent with the mandates of the Appointments Clause of Article II. U.S. Const. art. II, § 2, cl. 2.

An undeniable aspect of America today is its modern administrative state. This extraconstitutional body wields great power, in large part by means of what commentators have labeled a "hidden judiciary." *See* Kent Barnett, "Against Administrative Judges," 49 *UC Davis Law Review* 1643, 1645 (2016) (quotations and citations omitted). There are reportedly a total of 1,792 administrative law judges in service to federal agencies today. 1,537 Social Security Administration ALJs alone "collectively handle hundreds of thousands of hearings a year." *Bandimere v. SEC*, 844 F.3d 1168, 1199 and 1199 n.5 and n.6 (10th Cir. 2016) (McKay, J., dissenting) (citations omitted), *petition for certiorari pending sub nom.* ___ U.S. ___ (No. 17-475) (filed September 29, 2017).

Such facts are already well known to the Court. *See Free Enterprise Fund v. Public Company Accounting Oversight Board*, 561 U.S. 477, 586 app. C (2010) (Breyer, J., dissenting) (noting in excess of 1,500 ALJs in the employ of the federal government at that time). The above statistics regarding Social Security Administration adjudicators provide but one pungent example of the pervasive influence of appointed ALJs over the everyday lives of ordinary Americans. This lends credence to the statement that "[t]oo many important decisions of the Federal Government are made nowadays by unelected officials." *Environmental Protection Agency v. EME Homer City Generation, L.P.*, 572 U.S. ___, ___, 134 S. Ct. 1584, 1610 (2014) (Scalia, J., dissenting).

Equally so, administrative agencies today are rightly said to comprise the "fourth branch of the U.S. Government," exerting significant power over the economic and social life of the Nation. *PHH Corp. v. Consumer Financial Protection Bureau*, 839 F.3d 1, 6 (D.C. Cir. 2016) ("*PHH I*"), *vacated, reinstated in part, and remanded*, ___ F.3d ___, 2018 WL 627055 (D.C. Cir. January 31, 2018) (*en banc*). Agencies and their nonjudicial arbiters represent one side of a conflict between "executive power and individual liberty." *PHH I*, *supra*, 839 F.3d at 5. If administrative law judges are left unrestrained, they can pose a "significant threat" to bedrock principles of separation of powers and checks and balances. *PHH I*, *supra*, 839 F.3d at 6.

The drafters of the Founding Documents could not have foreseen contemporary SEC ALJs, *Bandimere*, *supra*, 844 F.3d at 1170, nor, in all likelihood, the latter's numerous peers presently at work within the far-flung bureaucracy extant today. It is equally unlikely the Framers envisioned these administrative adjudicators outnumbering the Article III bench by a ratio of two to one. *See* http://www.uscourts.gov/judges-judgeships-authorized-judgeships (last visited January 19, 2018) (860 authorized judgeships for 2016).

Nevertheless, the founders did hold dear a justifiable concern for executive power concentrated in the hands of the one or the few, and, worse yet, such authority lacking accountability to the political will of the citizenry. It was this "fear that prompted the Framers to build checks and balances into our constitutional structure." *Dep't of Transportation v. Association of*

American Railroads, 575 U.S. ___, ___, 135 S. Ct. 1225, 1244 (2015) (Thomas, J., concurring in the judgment).

Thus, the authors of the Constitution wisely safeguarded our ordered system of liberty. The Framers did so with a fundamental and inarguable precept in mind. "Liberty requires accountability." *Id.*, 575 U.S. at ___, 135 S. Ct. at 1234 (Alito, J., concurring).

The foregoing maxim animates the Appointments Clause. U.S. Const. art. II, § 2, cl. 2. Above all else, the Clause insists that those who wield executive authority remain "accountable to political force and the will of the people." *Freytag v. Commissioner of Internal Revenue*, 501 U.S. 868, 884 (1991). In regulating the manner of taking office, the proviso assures that ALJs (and, to a fair degree, their respective administrative agencies) are "accountable to the President, who himself is accountable to the people." *Dep't of Transportation*, *supra*, 575 U.S. at ___ 135 S. Ct. at 1238 (Alito, J., concurring). The Appointments Clause is one of several "accountability checkpoints" which secure separation of powers and checks and balances. *Id.*, 575 U.S. at ___, 135 S. Ct. at 1237 (Alito, J., concurring).

The case at bar encompasses a potential threat to accountability, and, consequently, individual liberty, a threat that is well familiar to the Court. Once more, the "wolf comes as a wolf." *Morrison v. Olson*, 487 U.S. 654, 699 (1988) (Scalia, J., dissenting), *quoted by PHH I*, *supra*, 839 F.3d at 8. The resolution of the instant case shall forge yet another adamantine link in the

chain of precedents upholding inviolate axioms of checks and balances and separation of powers. *See Morrison*, *supra*, 487 U.S. at 697 (1988) (Scalia, J., dissenting).

It is a constitutional imperative that *all* ALJs at *all* administrative agencies attain and hold office in conformity with the Appointments Clause, and thereby honor the Framers' "dedication" and "devotion to the separation of powers." *Dep't of Transportation*, *supra*, 575 U.S. at ___, 135 S. Ct. at 144 (Thomas, J., concurring in the judgment). That is why the matter at hand is not necessarily delimited to SEC ALJs nor the Commission. Whenever the Appointments Clause is called into question, inevitably there are "systemic ramifications" for all administrative agencies. *PHH I*, *supra*, 839 F.3d at 9 n.5.

For all these reasons, this *amicus curiae* respectfully suggests that a robust and definitive interpretation of the Appointments Clause in the case at bar shall clarify the constitutionality of the appointment process for all ALJs across all federal agencies, and thereby cabin executive power in accordance with fundamental precepts of separation of powers and checks and balances.

II. THE COURT MUST ASSURE THAT *FREE ENTERPRISE FUND* IS CORRECTLY APPLIED BY THE LOWER COURTS.

For nearly a decade now, *Free Enterprise Fund*, *supra*, has been the pivot upon which Appointments

Clause controversies have turned. *See, i.e., PHH I, supra*, 839 F.3d at 7. The Appointments Clause itself is a "structural safeguard" that tethers federal officers to the "sovereign power of the United States, and thus to the people." *Bandimere, supra*, 844 F.3d at 1188 (Briscoe, J., concurring).

Notwithstanding the Court's clear articulation of guiding principles in *Free Enterprise Fund*, the case at bar exemplifies that the lower courts still grapple with a correct reading of that precedent. *See, i.e., Hill v. SEC*, 825 F.3d 1236, 1247-48 (11th Cir. 2016) (the complainant was "not in the type of precarious position the Supreme Court found unacceptable in *Free Enterprise Fund*"); *Bennett v. SEC*, 844 F.3d 174, 182 and 186 (4th Cir. 2016) (distinguishing on the facts, and declaring the plaintiff "reads too much into" and further "misreads" *Free Enterprise Fund*).

Indeed, one such troubling misapprehension of *Free Enterprise Fund* was displayed very recently in *PHH Corp. v. Consumer Financial Protection Bureau*, ___ F.3d ___, 2018 WL 627055 (D.C. Cir. January 31, 2018) (*en banc*) ("*PHH II*"). There, the *en banc* D.C. Circuit seemingly conflated multi-member administrative commissions with an agency controlled by a solitary head. *Id.*, ___ F.3d at _, slip op. at 9 and 32-33 (declaring as "untenable" any claim of a constitutional distinction between the CFPB's single director and "multi-member independent agencies," including amongst the latter the Securities and Exchange Commission, the Federal Trade Commission, and the Federal Reserve).

The reasoning of the *PHH II* court was substantially grounded upon its interpretation of *Free Enterprise Fund*. *PHH II*, ___ F.3d at ___ and ___, slip op. at 19-20 and 26-30. This is further evidence that the lower courts continue to struggle with ascertaining the true import of *Free Enterprise Fund*, and then correctly applying that landmark to Appointment Clause controversies.

It is of paramount importance that any misconceptions held by the courts of appeals regarding the meaning of *Free Enterprise Fund* be brought to an end. The need for such clarity is comprised of elements both specific and general.

With respect to the former, the federal securities laws assure disclosure, transparency, and honesty in our vital capital markets. *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 170-71 (1994). SEC ALJs play a major role in upholding that paradigm. The Court's decision in the case at bar shall ensure that Commission adjudicators henceforth fulfill their important role in the scheme of federal securities regulation in a manner consistent with *Free Enterprise Fund*.

Regarding the latter, and as already ably demonstrated in the preceding section, SEC ALJs are but one small component of the vast federal administrative construct. The Court's resolution of the matter at hand will further refine the teachings of *Free Enterprise Fund*, and thereby assure that all in-house adjudicators at a

multitude of agencies hold office in accord with the strictures of the Appointments Clause.

It must be remembered that *Free Enterprise Fund* is a major fortification, erected to safeguard separation of powers and checks and balances. In an era of an ever-sprawling nationwide bureaucracy, the two circuit cases directly relevant to the case at bar, as well as others discussed herein, reveal a troubling disparity in the lower courts' apprehension of that important precedent, at least with regard to the status of SEC ALJs, and possibly with respect to other administrative adjudicators.

For reason of the preceding, this *amicus curiae* respectfully suggests the Court's resolution of the question presented shall assure that *Free Enterprise Fund* is correctly applied by the lower courts.

III. THE COURT'S DECISION SHALL END THE INTERNECINE CIRCUIT CONFLICT OVER THE CONSTITUTIONALITY OF THE APPOINTMENT PROCESS FOR SEC ALJs.

In the wake of the Great Recession, remedial legislation "dramatically expanded" the authority of the SEC to bring enforcement actions before its in-house ALJs. *Tilton v. SEC*, 824 F.3d 276, 278-79 (2d Cir. 2016), *cert. denied*, ___ U.S. ___, 137 S. Ct. 2187 (2017). Respondents in such cases were thus provoked to vigorously contest the power of the Commission's adjudicators to preside over these proceedings. *Id.*, 824 F.3d at 279. Such challenges nearly always invoked the

holding of *Free Enterprise Fund*, *supra*, 561 U.S. at 484, in support of the argument that, identical to the accounting industry oversight board members implicated in the aforementioned landmark, SEC ALJs likewise hold office in violation of the Appointments Clause of Article II. U.S. Const. art. II, § 2, cl. 2.

The instant controversy's first iteration resulted in a significant number of conflicting district court decisions. *See generally* Michael A. Sabino & Anthony Michael Sabino, "Challenging the Power of SEC ALJs: A Constitutional Crisis or a More Nuanced Approach?" 43 *Securities Regulation Law Journal* 369 (2015) (analyzing the then-extant cases). As these lower court controversies percolated to the appellate level, this divisiveness only increased, as a veritable legion of circuit court decisions evinced a deepening conflict.

One aspect of that division is before the Court today: the irreconcilable differences between the instant case and ruling of *Bandimere*, *supra*, 844 F.3d at 1182 (expressly disagreeing with the holding below in the case at bar). To be sure, Petitioners are irrefutably correct in calling attention to this clash of two key adjudicative bodies. Yet the disharmony amongst the appellate courts extends well beyond the two tribunals already mentioned.

When confronted by essentially the same scenario undergirding the instant case, a significant number of other circuits avoided the Appointments Clause question altogether, and confined their rulings to

jurisdictional grounds. *Bebo v. SEC*, 799 F.3d 765, 767-68 (7th Cir. 2015), *cert. denied*, ___ U.S. ___, 136 S. Ct. 1500 (2016); *Jarkesy v. SEC*, 803 F.3d 9, 29-30 (D.C. Cir. 2015); *Tilton, supra*, 824 F.3d at 279 and 291; *Hill, supra*, 825 F.3d at 1237 and 1241; *and Bennett, supra*, 844 F.3d at 176 and 183.

Yet even within that subset of relevant holdings, the rationales proffered by the respective tribunals lack cohesion. *Compare Tilton, supra*, 824 F.3d at 279 and 282 (apparently giving equal weight to all three jurisdictional factors promulgated in *Thunder Basin Coal Co. v. Reich*, 501 U.S. 200 (1994), and further emphasizing the "closer questions" presented therein on the last two legs of the *Thunder Basin* test); *Hill, supra*, 825 F.3d at 1250 (finding the last two factors of *Thunder Basin* "do not cut strongly either way and thus do not persuade us"); *Bennett, supra*, 844 F.3d at 183 and 183 n.7 (while seeming to consider all three *Thunder Basin* factors, nevertheless declaring in a parenthetical the first element of *Thunder Basin* is "the most important"); *Jarkesy, supra*, 803 F.3d at 22 (*Thunder Basin* is comprised of mere "guideposts for a holistic analysis"); *and Bebo, supra*, 799 F.3d at 773 (emphasizing the importance of *Elgin v. Dep't of Treasury*, 567 U.S. 1 (2012), to its jurisdictional analysis).

This plethora of appellate rulings demonstrates a pronounced dissonance amongst the Nation's tribunals which have confronted substantially the same circumstances as found in the case at bar. Even more troubling, and notwithstanding the diversity of methodologies employed, the decisions catalogued above do

share one key ingredient: each circuit panel avoided the precise Appointments Clause question presented in the matter at hand.

The existing disharmony might be propagated by the fact that some, if not all, of the holdings set forth above are beyond further scrutiny. Quite exemplary is the recent conclusion of the enforcement action underlying *Tilton*, *supra*. A subsequent decision by a Commission ALJ dismissed all charges. *In the Matter of Tilton, et al.*, Admin. Proc. File No. 3-16462 at 1 and 57 (September 27, 2017) (Foelak, A.L.J.). This development obviously forecloses further appellate review. Similar fates may yet follow for the other cases set forth hereinabove, placing a reconciliation between the differing circuits beyond reach.

In sum, essentially half of the circuit courts are effectively balkanized on the Appointments Clause question presented. Any opportunity for consensus at the level of the lower tribunals is well past. That reveals the true danger here: the prospect of additional appellate decisions inconsistently resolving the subject at issue, in holdings that might very well conflict with the Court's established Article II jurisprudence.

For these reasons, this *amicus curiae* respectfully suggests that the Court's explicit decision herein shall end the internecine circuit conflict over the constitutionality of the appointment process for SEC ALJs.

CONCLUSION

Respectfully, for all the reasons set forth above, the Court should resolve the question presented, and hold for Petitioners.

Respectfully submitted,

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SECURITIES AND EXCHANGE COMMISSION

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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INTRODUCTION AND INTERESTS OF *AMICI*[1]

In 1798, Thomas Dunn served as Assistant Doorkeeper of the House of Representatives, charged with, among other things, keeping the House's fireplace stocked with firewood and doing standard janitorial work. For these services, Congress paid him "four hundred and fifty dollars per annum."[2] And because of these ministerial services, Congress called him an "*officer* of the House of Representatives." Act of March 2, 1799, ch. 33, 5 Stat. 728 (emphasis added). This historical example of the founding-era usage of "officer" is merely one of many data points for the Court to consider in answering the important question presented in this case—the meaning of the phrase "officer of the United States."

Amici (listed in the Appendix) are scholars of a developing methodology for answering such questions in a systematic, rigorous manner—a methodology known as "corpus linguistics." As Utah Supreme Court Justice Thomas R. Lee puts it,, "corpus linguistics is an empirical approach to the study of language that involves large, electronic databases," which are used to "draw inferences about language from data gleaned

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[1] No one other than *amici* and their counsel authored any part of this brief or made a monetary contribution to fund its preparation or submission. All parties have consented to its filing in communications on file with the Clerk.

[2] Act of April 12, 1792, ch. 20, 2 Stat. 252 . See also Act of July 16, 1798, ch. 81, 5 Stat. 608 (appointing Dunn).

from real-world language in its natural habitat—in books, magazines, newspapers, and even transcripts of spoken language."[3] Because judges—like linguists and lexicographers—are interested in the "original public meaning" of historic texts and the "ordinary meaning" of modern texts, *amici* believe these databases can be invaluable in resolving difficult questions of constitutional and statutory interpretation.

Empirical evidence derived from historical databases demonstrates that Dunn's status as a federal officer—despite having little authority over anything but the Congressional fireplace—was not an aberration, but rather emblematic of the original understanding of "Officers of the United States." Moreover, linguistic data derived from a modern linguistic database reveals that our contemporary understanding of the word "officer" is far more expansive than some might expect—at least in the public context—encompassing relatively low-level employees.

Thus far, this Court's decisions have always reflected this broad understanding of "Officers of the United States." In *Landry* v. *FDIC*, 204 F.3d 1125, 340 (D.C. Cir. 2000), however, the D.C. Circuit fashioned a balancing test that does not adequately account for this Court's precedent, much less the available linguistic evidence. Because the *Landry* test—and similar tests from other circuits—have no grounding in linguistic fact, *amici* believe they should be overturned in favor of a more capacious understanding of the term "officer" and, hence, of the phrase "officer of the United States."

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[3] Lee & Mouritsen, at 788.

STATEMENT

The Constitution provides that the President "by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other *Officers of the United States*." U.S. Const., art. II, § 2. Nevertheless, "Congress may by Law vest the Appointment of such inferior Officers . . . in the President alone, in the Courts of Law, or in the Heads of Department." *Id.* Thus, an "Officer of the United States" may be appointed by any of three entities: the President (with or without Senate confirmation), the courts, or a department head.

1. However, administrative law judges are not appointed by the President, courts of law, or department heads. Rather, they are hired following a "merit-selection process" that is "administered by the Office of Personnel Management [OPM]." *Bandimere* v. *SEC*, 855 F.3d 1128, 1132 (10th Cir. 2017), en banc denied, 855 F.3d 1128 (Lucero, J., dissenting from denial of en banc review) (citing 5 U.S.C. 1302; 5 C.F.R. § 930.201). OPM requires a candidate to be a "licensed attorney[] with at least seven years of litigation experience" and to take a test that it administers. *Bandimere* v. *SEC*, 844 F.3d 1168, 1176-1177 & n.11 (10th Cir. 2016),[4] en banc denied, 855 F.3d 1128. Following the test's administration, each candidate is ranked according to his or her performance, and the Chief ALJ can then

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[4] For this proposition, the opinion cites Vanessa K. Burrows, Cong. Res. Serv., Administrative Law Judges: An Overview, at 2 (2010), https://perma.cc/T8YY-EE7F; Robin J. Arzt et al., *Advancing the Judicial Independence and Efficiency of the Administrative Judiciary: A Report to the President-Elect of the United States*, 29 J. Nat'l Ass'n Admin. L. Judiciary 93, 101 (2009).

hire any of the top three performers. *Id.* Once hired, ALJs are subject to termination only for cause after review by the Merit System Protection Board. *Id.* Their responsibilities include "conducting public hearings in a manner similar to federal bench trials," "presiding at and regulating the course of th[ose] hearings," and "setting filling deadlines, issuing subpoenas, holding prehearing conferences, and ruling on motions."[5]

2. Petitioner Raymond J. Lucia is an investor who has hosted several free seminars on investing. Pet. App. 34a; 127a–129a. At these seminars, Petitioner would use a slideshow to show the potential of following a retirement plan that he called "Buckets of Money." Pet. App. 23a; 127a–129a. The slideshow presented multiple "hypothetical" examples of how successful a portfolio following his plan could be.

Petitioner did not, however, only call his examples "hypothetical." Instead, he stressed both orally and in writing that they were based on many different assumptions, including assumptions that the history of the market was indicative of its future. Pet. App. 24a–29a; 43a n.10; 45a n.14; 76a–77a.

3. These disclosures, however, were insufficient to protect him from the Securities and Exchange Commission (SEC). In 2012, the SEC charged him with violating the Investment Advisors Act of 1940 and its subsequent interpretations of the Act. Pet. App. 7a–8a. The SEC chose to avoid federal court, and an administrative law judge presided over a trial-like proceeding that included all of the elements of a typical

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[5] U.S. Security and Exchange Commission, *Office of Administrative Law Judges*, https://www.sec.gov/alj.

trial. Pet. App. 239a. Although the case was eventually remanded for further factual findings, the ALJ eventually found Lucia's presentations misleading because he used "'backtest' —a term with no statutory or regulatory definition"—to describe his investment plan. Pet. Br. 6. Petitioner described the "backtest" as the combination of "historical data" and certain "assumptions for other variables, such as inflation and real-estate rates of return." Pet. Br. 5. Because of the supposedly misleading nature of the term, the ALJ "barred Mr. Lucia from working as an investment advisor for the rest of his life, revoked his company's registration, and assessed civil penalties." Pet. Br. 6.

Lucia sought review from the full Commission. He challenged the ALJ's decision on the merits and also argued that the ALJ's office violated the Appointments Clause. Pet. App. 38a–40a. The Commission sustained the ALJ's finding and concluded that SEC ALJs are "not subject to the Appointments Clause." Pet. App. 66a-69a; 86a. It reasoned that SEC ALJs are not inferior officers because their decisions are not "effective and final" until the SEC itself files a "finality order." Pet. App. 90a.

4. A panel of the D.C. Circuit, relying on *Landry* v. *FDIC*, 204 F.3d 1125 (D.C. Cir. 2000), held that the SEC ALJ was an employee but not an "inferior officer." *Lucia* v. *SEC*, 832 F.3d 277, 289 (D.C. Cir. 2016), Pet. App. 21a. *Landry* discussed three "criteria" for courts to consider when distinguishing between inferior officers and employees: "(1) the significance of the matters resolved by the officials, (2) the discretion they exercise in reaching their decisions, and (3) the finality of those decisions." *Tucker* v. *Comm'r*, 676 F.3d 1129, 1133 (D.C. Cir. 2012).

Petitioner showed that the SEC ALJ's decision, while not binding on the Commission, should not be considered a mere recommendation because, in practice, the Commission's eventual decision was only a "ministerial formality." *Lucia*, 832 F.3d at 286. The court recognized that, although under the organic statute "the Commission *could* have chosen to adopt regulations whereby an ALJ's initial decision would be deemed a final decision of the Commission," it had not. *Id.* (italics in original). Thus, under the current regulatory scheme, the SEC ALJ's decision "becomes final when, and only when, the Commission issues the finality order, and not before then." *Id.* Thus, the court held, the Commission's ALJs neither have been delegated sovereign authority to act independently of the Commission nor, by other means established by Congress, do they have the power to bind third parties, or the government itself, for the public benefit." *Id.*

While recognizing that "*Landry* ... did not resolve the constitutional status of ALJs for all agencies," the court below held that Petitioner "failed to demonstrate" that SEC ALJs "perform ... duties" sufficient to render them inferior officers. *Id.* at 289. For this reason, the court was unwilling to "cast aside [the] carefully devised scheme stablished after years of legislative consideration and agency implementation" and held that SEC ALJs were mere employees. *Id.*

The D.C. Circuit reheard the case *en banc*, agreeing to resolve the question of whether the ALJ was an inferior officer and therefore subject to the Appointments Clause. Pet. Br. 9. The *en banc* court convened on May 24, 2017. Pet. Br. 9. Equally divided, the *en banc* court issued a *per curiam* opinion denying the petition for review. Pet. App. 1a–2a.

SUMMARY OF ARGUMENT

Petitioners argue that the SEC's administrative law judges should be considered "Officers of the United States" under this Court's precedent, including *Buckley* v. *Valeo*, 424 U.S. 1 (1976). Petitioners' reading of those precedents is strongly supported by a technique called corpus linguistics—the use of electronically-searchable linguistic databases to generate empirical evidence about the meaning of words within in a particular community at a particular time. Application of that methodology shows that the D.C. Circuit's *Landry* test—and similar tests in other circuits—reflects neither the original nor modern meaning of the phrase "Officer of the United States." The Court should reject the *Landry* test in favor of a more capacious understanding of the term.

I. Empirical evidence demonstrates that "Officer of the United States" was not a legal term of art, that its original public meaning was much more expansive than the D.C. Circuit's case law affords, and that it referred to almost any federal employee. That evidence is principally derived from an analysis of the Corpus of Founding Era American English (COFEA)—a huge database containing approximately 150,000 documents from the Revolutionary War era—and a smaller database, created specifically for this case, consisting of all the Statutes-at-Large passed by the first Five Congresses between 1789 and 1799. Among others, these databases reveal references to the following federal "officers":

- The Assistant Doorkeeper of the House of Representatives;
- The Melter and Refiner of the U.S. Mint;

- The Deputy Apothecary of the U.S. Army; and
- The Purveyor of Public Supplies.

If this Court were to apply the original public meaning of the phrase "Officers of the United States," it would almost certainly extend to administrative law judges.

II. Empirical evidence also demonstrates that modern usage of the word "officer"—at least within the public sphere—continues to track the much more expansive original public meaning. To conduct the modern linguistic analysis, *amici* relied on the Corpus of Contemporary American English (COCA), a 560+ million word database capturing actual usages from 1990 to 2017. This corpus search revealed a number of low-level government employees referred to as "officers" that would nonetheless fail the *Landry* test:

- Archaeological preservation Officers (National Parks);
- Foreign Service Officers (State Department);
- Problem Resolution Officers (IRS);
- Safety Officers (FDA); and
- Wildlife Officers (National Park).

Based on this evidence, it is clear that the circuit courts' understanding of the "significant authority" test is also at odds with modern usage of "officer." If the court applied today's ordinary meaning of that word, it would easily extend to administrative law judges because, although their decisions may not be

final, they exercise a non-negligible degree of authority.

ARGUMENT

I. The Court should consider empirical evidence derived from corpus linguistics to inform its decision on the meaning of the Appointments Clause.

This Court has stated that "[t]he Constitution was written to be understood by the voters; its words and phrases were used in their normal and ordinary . . . meaning." *United States* v. *Sprague*, 282 U.S. 716, 731 (1931). At times, the court has indicated that this means constitutional provisions should be interpreted as they were understood by "ordinary citizens of the founding generation." *District of Columbia* v. *Heller*, 554 U.S. 570, 577 (2008). Other times, the Court has relied on a modern interpretation of the text, stating that the meaning of the Constitution is not "static," but rather informed by "evolving standards of decency." *Trop* v. *Dulles*, 356 U.S. 86, 100–101 (1958); see also Stephen Breyer, Active Liberty: Interpreting Our Democratic Constitution 7–8 (2005). Regardless of its approach, the Court would benefit from the use of empirical data produced by corpus linguistic tools.

1. Corpus linguistics investigates real-language use and function by analyzing huge electronic databases of naturally-occurring texts. Thomas R. Lee & Stephen C. Mouritsen, *Judging Ordinary Meaning*, 127 Yale L.J. 788 (hereinafter Lee & Mouritsen)(2018). These databases have an esoteric name—corpora (the plural of corpus)—but are simply digitally-searchable collections of real-world sources: books, newspapers, speeches, scholarly articles, television transcripts, etc. *Id.* at 33. The sources are said to occur "naturally" because they "were not elicited for the purpose of the study. That is . . . no one ask[ed] the

speakers or writers whose words are represented in the corpus to speak or write for the purpose of subjecting their words to linguistic scrutiny. Instead, the architect of the corpus assemble[d] her collection of speech and writing samples after the fact." Stephen C. Mouritsen, *The Dictionary is not a Fortress: Definitional Fallacies and a Corpus-Based Approach to Plain Meaning*, 2010 B.Y.U L. Rev. 1915, 1954–1955.

Although corpus linguists use many different tools, when interpreting a historical text scholars often follow the following procedure:

- Identify a corpus that corresponds with the speech community and time period she wishes to investigate;
- Search for the relevant search term using a "Keyword in Context" (KWIC) feature, which finds and displays in context every instance of the queried term in the database;
- Generate a random (and thus likely representative) sample of the returned KWIC lines large enough to generate statistically significant effects; and
- Code each KWIC line in the sample for its relevant word sense, relying on the system's expanded context feature when necessary.[6]

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[6] See, *e.g.*, James Cleith Phillips & Jesse Egbert, *Advancing Law & Corpus Linguistics*, 2018 B.Y.U. L. Rev. (forthcoming), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3057415.

This approach can produce useful quantitative and qualitative data about the real-world usage of the relevant term.

It bears emphasis, however, that the sources contained in the corpus must be pulled from the relevant speech community being investigated. James Cleith Phillips & Sara White, *The Meaning of the Three Emoluments Clauses in the U.S.* Constitution, ___ S. Tex. L. Rev. (forthcoming 2018), *available at* https://ssrn.com/abstract=3036938. A corpus composed entirely of the transcripts from Argentinian telenovelas cannot provide relevant data for investigating the speech patterns of American diplomats. Likewise, a 16th century Shakespearean corpus will likely be unhelpful in clarifying the meaning of modern legal texts. But a corpus that is contextually relevant "is like Lexis on steroids." Brief for Open Government Project as Amicus Curiae at 14, *FCC* v. *AT&T Inc.*, 562 U.S. 397 (2011). Searching it for a particular term produces a set of real-world examples (called "KWIC" or "concordance lines") drawn from the database and showing how that term has actually been used within the community in question.

Of course, not all of the examples produced by the corpus will be helpful. Like Google or Westlaw, a corpus search will sometimes identify sources in which the queried term was used in a very different context. Other times the usage will be vague or ambiguous. But analyzing a random sample of concordance lines, as a whole, produces a broader empirical picture, defining the range of potential meanings a word or phrase may take and often revealing trends and patterns that would have otherwise remained unnoticed.

2. This approach should feel familiar to most judges. Courts search for real-world examples of linguistic usage to help make sense of ambiguous legal passages all the time. For example, in *Heller*, this Court considered concrete examples mined from "founding era sources" of how the phrases "keep arms" and "bear arms" were actually used by contemporaries of the Constitution. 554 U.S. at 581-592.

The problem is that until now "a judge has [had] no way of determining whether she is correct in her assessment that her own interpretation is widely shared." Lawrence Solan, *et. al.*, *False Consensus Bias in Contract Interpretation*, 108 Colum. L. Rev. 1268, 1273 (2001). Linguists have long noted the fallibility of human linguistic intuition. Because "humans tend to notice unusual occurrences [of words] more than typical ones," judges run the risk of over-crediting the frequency of obscure word senses. Douglas Biber et. al., Corpus Linguistics: Investigating Language Structure and Use 3 (1998).

To combat this, some judges have turned to electronic databases to help generate more examples of real-world usage than they can think of on their own, as a way to check their linguistic intuition. This Court did so in *Muscarello* v. *United States*, "survey[ing] modern press usage [of the word "carry"] by searching computerized newspaper databases." 524 U.S. 125, 129-130 (1998). Likewise, in *United States* v. *Costello*, Judge Posner performed a Google search "of several terms in which the word 'harboring' appears" on the "supposition that the number of hits per term is a rough index of the frequency of its use." 666 F.3d 1040, 1044 (7th Cir. 2012). While these approaches had

some methodological shortcomings,[7] they are laudable for their efforts to check the court's linguistic assumptions.

Corpus linguistics simply empowers the judge to do this in a systematic—and more scientific—fashion: systematic because it follows a set methodology and relies on principles of statistical significance and random samples; and scientific because it is both falsifiable and repeatable: subsequent researchers can test the validity of any dataset by performing the corpus search again on their own. This approach does not supplant the judge as the ultimate decision maker. It simply furnishes the judge with more and better data to help inform her ultimate decision.

3. Over the last few years, some judges have cautiously begun applying corpus linguistic tools and techniques to issues of statutory interpretation. For example, in 2011 Justice Ginsburg cited corpus linguistics data during oral arguments in *FCC* v. *AT&T, Inc.*, 562 U.S. 397 (2011). See Transcript of Oral Argument in No. 09-1279 at 37. The case boiled down to whether the word "personal" as used in the Freedom of Information Act was merely the 'adjectival form' "of the noun person" so that the phrase "personal privacy" encompassed corporate privacy. See 562 U.S. at 406. While the opinion did not cite corpus linguistics directly, its reasoning largely tracked the amicus brief by the Project on Government Oversight, which did.

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[7] See, *e.g. Muscarello*, 524 U.S. at 129 (Breyer, J.) (describing his own empirical approach as "crude[]"); *State* v. *Rasabout*, 356 P.3d 1258, 1280 (Utah 2015) (Lee, J. concurring) (critiquing Judge Posner's reliance on Google searches); Lee & Mouritsen, at 812-813 (same).

That same year, Justice Lee of the Utah Supreme Court became the first judge in the country to expressly use corpus linguistics in an opinion. *In re Adoption of Baby E.Z.*, 266 P.3d 702 (Utah 2011) (Lee, J. concurring). Relying on empirical data drawn from Brigham Young University's Corpus of Contemporary American English (COCA),[8] he concluded that the term "custody determination" as used in the federal Parental Kidnapping Prevention Act did not extend to adoption proceedings because "the most common family-law sense of the word 'custody' occurs in the setting of a divorce." *Id.* at 724.

Since then, a number of state supreme court justices have followed suit.[9] For example, the majority and dissent in *People* v. *Harris*, a Michigan Supreme Court case in which both the majority and dissent relied on the COCA to analyze whether someone had been forced to make an involuntary statement if the "information" he provided law enforcement officers was actually false. 885 N.W.2d 832.[10]

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[8] Corpus of Contemporary American English, https://corpus.byu.edu/coca/.

[9] See, *e.g.*, *Fire Ins. Exchange* v. *Oltmanns*, —___ P.3d —___ (Utah 2017), 2017 UT 81 ¶57 n.9 (Durham, J. concurring) ("[Corpus linguistic] tools for empirical analysis are readily available for lawyers and should be used when appropriate"); *cf. State* v. *Canton*, 308 P.3d 517 (interpreting the phrase "out of the state" based on an analysis of the use of that phrase in newspaper articles compiled through a Google News search)

[10] Corpus linguistics has also been used to settle trademark disputes at the trial level for many years. See Barton Beebe & Jeanne C. Fromer, *Are We Running Out of Trademarks? An Empirical Study of Trademark Depletion & Congestion*, 131 Harv. L. Rev. 945 (2018).

4. Thus far, all these cases have involved the interpretation of modern statutes and have therefore relied on data derived from modern English corpora such as the COCA. But these tools are less helpful for cases involving constitutional interpretation, at least to the extent the Court is interested in discovering the meaning understood by "ordinary citizens of the founding generation." If one is interested in the original public meaning, a modern corpus is just as unhelpful as a corpus derived from sources from the wrong community—it fails to account for subsequent changes in language patterns. As Justice Lee has explained, "This is the problem of linguistic drift—the notion that language usage and meaning shifts over time." Thomas R. Lee & James Cleith Phillips, *Data-Driven Originalism*, *available at* http://ssrn.com/abstract=3036206 [hereinafter Lee & Phillips] .

Sometimes these changes can be quite dramatic, and occur for no apparent reason. Consider the following (possibly apocryphal) account of the rebuilding of St. Paul's Cathedral in 1675, taken from a linguistics column published during the early twentieth century:

> When architects' drawings for the rebuilding of St. Paul's Cathedral after the fire were submitted, Sir Christopher Wren was told that his design had been chosen because it was "at the same time the most awful and the most artificial." A modern architect would hardly think such a verdict complimentary. Far from being disparagement, it was the highest praise. "Awful" correctly meant inspiring awe, and "artificial" designed with art.

Arthur Ponsonby, *The King's English*, The Baltimore Sun, M15 (March 18, 1928); *see also* John W. Welch, *et. al. The Preamble's Principal Place in Constitutional Law*, 91 S. Cal. L. Rev. (forthcoming 2018), available at http://ssrn.com/abstract=3131207. Such shifts can—and have—occurred with words and phrases contained in the Constitution. For example, Article IV, Section 4 states that "[t]he United States . . . shall protect each of [the states] . . . against domestic violence." At the time of the founding, "domestic violence" referred to civil unrest and public upheaval rather than the abuse of one's spouse or children as it does today. Lee & Phillips at 4 .

5. Until recently, no eighteenth century American English corpus existed. But in late 2017, Brigham Young University Law School launched a beta version of the Corpus of Founding Era American English ("COFEA"). COFEA currently contains approximately 150 million words. The texts were mined from Evans Early American Imprint Series (featuring books, pamphlets, and broadsides covering a broad array of subjects), Hein Online's Legal Database, and the papers and correspondence of George Washington, Benjamin Franklin, John Adams, Thomas Jefferson, James Madison, and Alexander Hamilton, as contained in the National Archives Founders Online Project. Future versions of COFEA will include additional sources such as colonial newspapers, the Records of the Federal Convention of 1787, and the Documentary History of the Ratification of the Constitution. Lee & Phillips at 31.

In the sections that follow, we use COFEA and other founding era corpora to show that the original public meaning of the phrase "Officers of the United

States" encompassed significantly more employees than allowed under the D.C. Circuit's *Landry* test. We then use COCA to show that this original meaning has remained largely unchanged in the public context since the time of the Founding. Accordingly, the Court should reverse the D.C. Circuit's decision, and fashion a test that accords with either the original or modern meaning of the phrase, or both.

II. Empirical evidence from the Founding era shows that "Officers of the United States" was not a legal term of art.

The phrase "Officer(s) of the United States" appears in COFEA just 109 times between 1787 and 1799, with just over a third of those being direct quotations of the Constitution.[11] This is a tiny minority of the 5,353 times the word "officer" appears in the database overall during this same period—even though 59.8% of the time the word "officer" appears in COFEA it is clearly referencing a federal employee.

1. While the relative obscurity of the longer phrase does not prove that it was *not* a legal term of art at the time of the Founding, we perceive no specialized meaning attached to its use. Instead, the appellation was often used simply to clarify that the agent was in the employ of the federal government, as opposed to a private actor or employee of a state or territory.

For example, in a letter to George Washington, General Arthur St. Clair expressed concern that the

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[11] Our raw data can be accessed at goo.gl/7xt8XP under the "COFEA 'Officers of the US' 1787-199" tab. To replicate our re-

Attorney General of the new Ohio territory "would be an Officer of the Territory only, whereas he should be an Officer of the United States." Likewise, Alexander Hamilton wrote to New York merchant William Seton, requesting he purchase public debt on behalf of the federal government since the government had yet to "employ some officer of the United States" for the task.

We do not see any linguistic evidence to suggest that the term was limited to only a small subclass of all federal officials. To the contrary, it applied broadly to all government employees—"civil and military" —exercising any non-trivial federal authority. For instance, in his Eighth Annual Address to Congress at the end of 1797, George Washington called for "legislative revision" of "[t]he compensation to the officers of the United States," particularly "in respect to the most important stations." Had "Officers of the United States" been understood to refer only to those federal employees with a significant degree of authority, as *Landry* suggests, there would be no need to give special emphasis to "the most important stations." Congress responded the following March, raising the salaries of sundry government officials, high and low. Act of March 19, 1798, ch. 18, 5 Stat. 542. Nevertheless, Congress did not use the phrase "Officers of the United States" in the appropriations bill, but instead referred generally to "officers," "offices," and "persons employed." *Id.*

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sults, search COFEA for "Officer of the United States" and "Officers of the United States" for the years 1787-1798. Corpus of Founding Era American English, BYU Law Corpora, https://lawncl.byu.edu/cofea/.

2. Our findings are buttressed by those of Professor Jennifer Mascott, who used aspects of corpus linguistics to demonstrate that the phrase "Officers of the United States" was in use prior to the creation of the Constitution. Jennifer L. Mascott, *Who Are "Officers of the United States"?* 70 Stan. L. Rev. 443 (2018). Using a corpus of 340,000 issues of early American newspapers, she found twenty uses of the phrase "prior to the signing of the Constitution on September 17, 1787." *Id.* at 478. The first reference was in 1780, describing Benedict Arnold as a "general officer of the United States." *Id.* It appeared again in 1783 referring simply to continental officers. Sometimes the phrase was used with "slight variations," showing the phrase was not a term of art. Other uses included "Judicial Officers of the United States" and "commissaries and other officers of the United States" who gave out certifications of debt under the Constitution. *Id.* at 479.

Professor Mascott also performed a corpus analysis of the Journals of the Continental Congress, "a highly relevant source for identifying the well-understood meaning of legally relevant terms and phrases in the time period just prior to...the drafting and ratification of the Constitution." *Id.* at 477. The Journals contain forty-one references to "officer(s) of the United States." Often the phrase was "just another way to describe continental military officers or to identify continental-level, as opposed to state-level, officers." *Id.* at 477-478. For example, one letter distinguished between the time a military officer served as an "officer of the United States" and time served as a captain for his State. *Id.* at 478 n.175.

But even if "Officers of the United States" was a legal term of art, its original meaning was much more

expansive than *Landry* imagines, and appears to have applied to all government employees—"civil and military" —exercising any degree of federal authority. COFEA similarly reveals that the term applied to not just high ranking government officials, but also customs officials,[12] loan officers,[13] and law enforcement officials carrying out warrants.[14]

III. Empirical evidence derived from corpus linguistics demonstrates that the original public meaning of "officer" would have encompassed an ALJ.

If we are correct that "Officers of the United States" was not a new legal term of art, then it is instead simply "a descriptive phrase indicating the officers are federal, and not state or private, actors." Mascott, at 471. The meaning of "officer" in the Constitution should thus correspond with the original public meaning of the term "officer" in general.

1. The word "officer" appears in COFEA 5,353 times between 1787 and 1799. Analysis of a random

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[12] *Letter from Alexander Hamilton to Robert Purviance* (August 22, 1794), *in* XVII The Papers of Alexander Hamilton 127 (Harold C. Syrett, ed., Colum. Univ. Press 1972).

[13] *Letter from Abishai Thomas to Alexander Hamilton* (June 14, 1792), *in* XI The Papers of Alexander Hamilton 520 (Harold C. Syrett, ed., Colum. Univ. Press 1966).

[14] Hugh H. Brackenridge, Incidents of Insurrection in the Western Parts of Pennsylvania, in the Year 1794 57 (1795), *available at* https://quod.lib.umich.edu/e/evans/N21549.0001.001?rgn=main;view=fulltext.

sample of 540 of these concordance lines[15] reveals the title was applied to a startling range of officials, including the President, Vice President, Speaker of the House, Secretary of State, Minister Resident to the Hague, U.S. Attorney, Collector, Naval Officer, auditor, excise officer, custom-house officer, and loan officer.[16]

We also created a specialized corpus of all Statutes-at-Large passed by the first five Congresses of the United States between 1789 and 1799. Congressional understanding of the word is particularly relevant because the Constitution delegates to Congress—and only Congress—the authority to deviate from the standard appointment process: while most officers were to be appointed by the President with the advice and consent of the Senate, "the Congress may by Law vest the Appointment of . . . inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments."

Ironically (given the year of the Constitutional Convention), the word "officer" appears in these statutes 1787 times, although that number goes down to 1411 when footnotes and sidebars—inserted by a later editor—are excluded. Of these 1055, or 74.8%, refer to civil officers; 311, or 22% refer to military officials; and 26, or just under 2%, refer to non-government employees. The remaining 1.3% of concordance lines were too

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[15] This sample gives us a 95% confidence interval with only a 4% margin of error.

[16] Raw data available at goo.gl/7xt8XP under the "'Officer' in Statutes-at-Large (1789-1799)" tab. Our results can be replicated by searching for "officer" in the Corpus of Founding Era Congressional Statutes. Corpus of Founding Era Congressional Statutes, BYU Law Corpora, https://lawncl.byu.edu/cofecs/.

ambiguous to code. The word was used in a number of contexts including the creation of new government positions, the enumeration of responsibilities, and the appropriation of funds.

As with the full phrase "Officers of the United States" the list of government employees referred to as "officers" is expansive. In addition to high-ranking officials such as the President, Vice President, and Secretary of State, specific enumerated officers included less glamorous positions such as the Purveyor of Public Supplies, the accountant of the War Office, and "the melter and refiner [of the U.S. Mint]." Each Port in the United States had three "customs officers" appointed by the President and confirmed by the Senate—a "Collector," "Naval Officer,"[17] and "Surveyor," whose duties included receiving ship manifests and inspecting imports. Even the "doorkeeper" and "assistant doorkeeper" of the House of Representatives—whose responsibilities included such important tasks as "tak[ing] care of the apartments occupied by the" House and "providing fuel and other accommodations" for Congressional sessions—were referred to as both "offices" and "officers"— —three times.[18]

Additionally, the corpus reveals that Congress created a small army of low-ranking government agents throughout the country—some appointed directly by

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[17] The term "naval officer" here can be deceptive to modern readers. It was a civil, not military, position within the Treasury Department. See Act of July 31, 1789, ch. 5, 1 Stat. 37.

[18] See Act of April 12, 1792, ch. 20, 2 Stat. 252.

the President[19] and others by heads of departments[20]—including "officers of inspection,"[21] "accounting officers,"[22] patent officers,[23] "revenue officers,"[24] "custom-house officers,"[25] "loan officers,"[26] "health officers,"[27] "recording officers,"[28] and "auxiliary officers."[29] The Treasury Department even appointed individual "officers" to survey each "distillery" and "still" of "spirits" in the Union.[30] Congress sometimes, but not always, referred to clerks and attendants as officers,[31] going as far as to require "each and every clerk and other officer . . . in any of the depart-

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[19] See, *e.g.* Act of Aug. 4, 1790, ch 35, 1 Stat. 175 (noting that the president appoints "officers of the customs")

[20] See, *e.g.* Act of Feb. 25, 1791, ch. 10, 1 Stat. 192 (empowering directors of the Bank of United States to appoint inferior officers).

[21] See, *e.g.* Act of Mar. 3, 1791, ch. 15, 1 Stat. 202.

[22] See, *e.g.* Act of Feb. 12, 1793, ch. 6, 2 Stat. 332.

[23] See, *e.g.* Act of Apr. 10, 1790, ch. 7, 1 Stat. 112.

[24] See, *e.g.*, Act of Mar. 26, 1794, ch. 2, 3 Stat. 400.

[25] See, *e.g.* Act of May 22, 1794, ch. 35, 3 Stat. 370.

[26] See, *e.g.* Act of March 14, 1794, ch. 6, 3 Stat. 343.

[27] See, *e.g.* Act of June 9, 1794, ch. 61, 3 Stat. 394 (consenting to Maryland's creation of s state health officer for the Port of Baltimore and allowing it to impose additional duties on imports to fund the position).

[28] See, *e.g.* Act of June 15, 1798, ch. 54, 5 Stat. 567.

[29] See, *e.g.* Act of July 11, 1798, ch. 71, 5 Stat. 591.

[30] Act of March 3, 1791, ch. 15, 1 Stat. 203-204.

[31] Act of Dec. 23, 1791, ch. 3, 2 Stat. 226.

ments of the United States . . .[to] take an oath or affirmation before one of the justices of the supreme court, or one of the judges of a district court of the United States, to support the constitution."[32] "Officers of the court," included clerks[33] and marshals.[34]

Within the military, there were two classes of "officers" —commissioned and non-commissioned. Commissioned officers, from lowly cornets up to major generals, received their commissions directly from the President. These included some surprising military positions, including chaplains,[35] deputy apothecaries[36] and "a competent number of hospital surgeons,"[37] who each had to be appointed in the same way "as other officers of the United States"—meaning nominated by the President and confirmed by the Senate. Act of March 2, 1799, ch. 27, 5 Stat. 721. Non-commissioned officers, however, were simply soldiers who had moved up through the ranks. They received no presidential commission or appointment, yet they were still considered "officers."

2. Once again, Professor Mascott's empirical work confirms these findings. Using a digitized version of Nathan Bailey's popular eighteenth-century dictionary as a corpus, she identified 500 sentences containing the word "office" or "officer." These included a

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[32] Act of March 3, 1791, ch. 18, 1 Stat. 215.

[33] Act of June 15, 1798, ch. 54, 5 Stat. 567.

[34] Act of March 2, 1799, ch. 22, 5 Stat. 696.

[35] Act of March 5, 1792, ch. 9, 2 Stat. 241.

[36] Act of March 2, 1799, ch. 27, 5 Stat. 721.

[37] *Id.*

number of record-keepers, assistants, and employees assigned menial tasks including:

> (i)The "Agistator" who took cattle into the forest; (ii) the "Chafe-Wax" who "fit[ted] the wax for the sealing of writs"; (iii) the "Expenditor," "a steward or officer, who look[ed] after the repairs of the banks of [a] [m]arsh"; (iv) the "Gauger" who measured liquids carried on a merchant ship; (v) the "Searcher" "whose business [was] to examine, and by a peculiar seal to mark the defects of woolen cloth"; and (vi) the "Swabber," "an inferior officer on board a ship o[f] war, whose office it [was] to take care that the ship be kept clean."

Id. at 492.

Mascott also notes that the term "officer" was used repeatedly in the Federalist and Anti-Federalist papers. Between them, the essays included over 600 uses of the terms "office(s)" or " officer(s)." *Id.* at 474. She asserts that the Anti-Federalists used the term "officer" to reference "rank-and-file officials." *Id.* at 52. For example, Brutus feared Congress's taxation power would lead to "the appointment of a swarm of revenue and excise officers to pray [sic] upon the honest and industrious part of the community . . . ." Brutus, *Federal Taxation and the Doctrine of Implied Powers (Part I)* (1787), *in* The Anti-Federalist Papers. Additionally, Richard Henry Lee wrote: "To discern the nature and extent of this power of appointments, we need only to consider the vast number of officers necessary to execute a national system in this extensive country." *An Anti-Federalist View of the Appointing Power Under the Constitution* (Federal Farmer XIII), *in* The Anti-

Federalist Papers. He also expressed that in the federal capital city, the only non-officer personnel category was that of "servant" or "attendant." *Id.*

The Federalists were not as concerned with the number of federal officers, but this is not because they did not believe the term "officer" accounted for almost all federal employees, but because they disagreed with the Anti-Federalist view that the federal government would be expansive. Mascott, at 502-503. Still, as Alexander Hamilton said: "As to persons to be employed in the collection of the revenues, it is unquestionably true that these will form a very considerable addition to the number of federal officers . . . ." The Federalist No. 84 (Alexander Hamilton).

3. Thus far, this Court's case law has always reflected this broad understanding of "Officers of the United States," acknowledging that even relatively minor government officials such as "a postmaster first class" and a "clerk of the district court" were "inferior officers of the United States within the meaning of the Appointments Clause."[38] Nevertheless, the circuit courts have become distracted by *Buckley*'s "significant authority" language, fashioning balancing tests that do not take into account past case law, much less

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[38] *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976); *Myers* v. *United States*, 272 U.S. 52 (1926) (holding that a "postmaster of the first class" was an "Officer of the United States"); *United States* v. *Germaine*, 99 U.S. 508, 509-510 (1879) ("[A]ll persons who can be said to hold an office under the government . . . were intended to be included within one or the other . . . modes of appointment [specified in the Constitution]."); *Ex parte Hennen*, 38 U.S. 225 (1839) (holding that law clerk was an inferior officer).

available linguistic evidence.[39] For example, in *Landry* v. *FDIC*, 204 F.3d 1125 (D.C. Cir. 2000), the D.C. Circuit established three "criteria" for courts to consider when distinguishing between inferior officers and employees: "(1) the significance of the matters resolved by the officials, (2) the discretion they exercise in reaching their decisions, and (3) the finality of those decisions." *Tucker* v. *Comm'r*, 676 F.3d 1129, 1133 (D.C. Cir. 2012). Using this test, the court concluded that administrative law judges—who "conduct public hearings in a manner similar to federal bench trials," "preside at and regulate the course of th[ose] hearings," and "set filling deadlines, issue subpoenas, hold prehearing conferences, and rule on motions"[40]—were not inferior officers.

But in light of this Court's precedent and the linguistic norms of the Founding era, a more accurate reading of the *Buckley* test is that an "Officer of the United States" is any federal employee that exercises

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[39] *Samuels, Kramer & Co.* v. *C.I.R.*, 930 F.2d 975, 986 (2d Cir. 1991) (examining the duties of the individual, whether the individual exercises discretion, and whether they perform important functions); *U.S. ex. rel. Kelly* v. *Boeing Co.*, 9 F.3d 743, 758 (9th Cir. 1993) (examining whether an individual has "primary responsibility" and "significant authority" to enforce the law); *Bandimere* v. *SEC*, 844 F.3d 1168 (10th Cir. 2016) (examining whether the position is established by law, whether the person exercises significant discretion in performing important functions, and whether the position's salary, duties, and means of appointment are determined by statute).

[40] U.S. Security and Exchange Commission, *Office of Administrative Law Judges*, https://www.sec.gov/alj.

non-negligible government authority. [41] If a judicial law clerk—not to mention the assistant doorkeeper of the House of Representatives—is an "Officer," surely an ALJ is, too.

IV. Empirical evidence derived from corpus linguistics demonstrates that the ordinary meaning of a public "officer" today includes ALJs.

Corpus linguistics analysis also demonstrates that the *Landry* test is at odds with the modern understanding of a public officer. Our findings show that the ordinary meaning of "officer" encompasses a host of employees whom the D.C. Circuit, using its current framework, would likely not classify as such. Specifically, the term "officer" includes public officials responsible for governmental duties of almost any level of significance.

1. To conduct our modern corpus analysis, we used the Corpus of Contemporary American English (COCA), a 560+ million word corpus capturing actual usages from 1990 to 2017. COCA is equally divided

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[41] Recent scholarship has suggested that a corpus analysis can be strengthened by investigating the relative frequency of the queried term's synonyms. See Lawrence M Solan & Tammy Gales, *Corpus Linguistics as a Tool in Legal Interpretation*, 2018 B.Y.U. L. Rev. ___ (forthcoming 2018) *available at* https://ssrn.com/abstract=3047150. One recent study found significant overlap in the use of the word "officer" and the phrase "public employment. James Cleith Phillips, *et. al.*, *Investigating the Original Meaning of 'Officers of the United States' with the Corpus of Founding-Era of American English, available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3126975.

among spoken, fiction, popular, magazines, newspapers, and academic texts. It strives to capture the full spectrum of American English—containing everything from scholarly medical journals to the transcripts of the Jerry Springer show.

Using COCA, we searched for the term "officer." That initial search resulted in 48,353 hits. From these results, we generated a statistically significant random sample of 604 concordance lines.[42]

Our analysis revealed a stark contrast between the use of the word "officer" in public and private contexts. For our purposes, the public context includes any level of government—be it federal, state, or local—while the private context includes all private entities, including business, non-profit, and religious organizations.

Only 18% of concordance lines referred to *private* officers. And analysis revealed that, in the context of business organizations, officers are "the most senior employees" and "are in charge of the day-to-day operations . . . mak[ing] many of the decisions that define a corporation's activities," D. Gordon Smith & Cynthia A. Williams, Business Organizations: Cases, Problems, and Case Studies 174 (3d ed. 2012). They are what we might refer to as the "top brass" of the organization, with titles that typically include the word "Chief"—Chief Executive Officer, Chief Financial Officer, General Counsel, etc.

But in the public context—represented by 78% of our sample—the original public meaning described

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[42] Raw data may be accessed at goo.gl/7xt8XP under the "'Officer' in COCA" tab. To replicate our results, search for "officer" in the Corpus of Contemporary American English. http://corpus.byu.edu/coca).

above still prevails, with "officer" referring to almost any public employee exercising a modicum of government authority. This is exemplified best in the many references to law enforcement—police officers, FBI agents, highway patrolmen, etc.—which make up 59% of our overall sample. Even the newest cop assigned to the traffic beat of the smallest police department is still referred to as an "officer."

But our sample is replete with other low-level government employees being referred to as "officer." On the federal level, these include: "archaeological protection officers" (National Parks),[43] "foreign service officers" (State Department),[44] "problem resolution

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[43] David Holmstrom, *A Summer Camp Where Community Service is Key*, Christian Science Monitor (Aug. 16, 1994), *available at* https://www.csmonitor.com/1994/0816/16101.html.

[44] See, *e.g.*, *Retired Marine Col. James C. Magee, 77, Dies*,, Wash. Post (Dec. 19, 1990), *available at* https://www.washingtonpost.com/archive/local/1990/12/19/retired-marine-col-james-c-magee-77-dies/643eef00-c905-4cb4-95d9-af6719cc39ec/?utm_term=.156253bbba87.

officers" (IRS),[45] "safety officers" (FDA),[46] "regional security officers" (State Department),[47] "intelligence officers" (CIA),[48] "wildlife officers" (National Parks),[49] and "contracting officer."[50] The umbrella is expanded when state and local usage is added to the mix: "prison

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[45] Elizabeth MacDonald, *Six Ways to Survive an IRS Audit*, Buffalo News (Sept. 11, 1994), *available at* http://buffalonews.com/1994/09/12/six-ways-to-survive-an-irs-audit/.

[46] Melissa Block, *Analysis: Lester Crawford officially named head of the FDA*, NPR: All Things Considered, Feb. 14, 2005.

[47] *Lives Could Have Been Saved in Benghazi*, Real Clear Politics Video (Sept. 8, 2013), *available at* https://www.realclearpolitics.com/video/2013/09/08/gregory_hicks_lives_could_have_been_saved_in_benghazi.html.

[48] See, *e.g.*, Robert O'Harrow Jr. et. al., *NSA Leaks Puts Focus on Intelligence Apparatus's Reliance on Outside Contractors*,. Wash. Post (June 10, 2013), *available at* https://www.washingtonpost.com/business/nsa-leaks-put-focus-on-in. lligence-apparatuss-reliance-on-outside-contractors/2013/06/10/e940c4ba-d20e-11e2-9f1a-1a7cdee20287_story.html?utm_term=.49d9427e6585.

[49] *Part I—Survival of the Wildest: Stopping Poachers in the Act*, CBS 48 Hours, Mar. 11, 1992.

[50] Steve Inskeep, *The Perfection of Character*, NPR (Oct. 23, 2006), *available at* https://www-s1.npr.org/templates/transcript/transcript.php?storyId=6352680.

officers,"[51] "animal control officers,"[52] "licensing officers,"[53] "truant officers,"[54] "water authority officers,"[55] "child welfare officers,"[56] "community service officers,"[57] "hearing officers,"[58] "placement officers,"[59] and

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[51] Ross B. MacDonals et. al., *The Politics of Victimhood*, 60 J. of Int'l Affairs 173 (2006), *available at* https://www.thefreelibrary.com/The+politics+of+victimhood%3A+historical+memory+and+peace+in+Spain+and+...-a0163049402.

[52] Richard Berman, *A Liberal Dose of State Ballot Measures*, Wash. Times (Nov. 7, 2016), *available at* https://www.washingtontimes.com/news/2016/nov/7/a-liberal-dose-of-state-ballot-measures/.

[53] Kenneth R. Timmerman, *Close-out Sale at Commerce*, 28 Am. Spectator 36 (Aug. 1995).

[54] *Truant Officers Attend to Schools' Needs*, Chicago Sun-Times, (Sept. 11, 1992).

[55] Allison Brown, *Counting Farmers Markets*, 91 Geog. Rev. 655 (Oct. 2001), *available at* https://www.questia.com/library/journal/1G1-93207326/counting-farmers-markets.

[56] Professor X, *In the Basement of the Ivory Tower*, Atlantic (June 2008), *available at* https://www.theatlantic.com/magazine/archive/2008/06/in-the-basement-of-the-ivory-tower/306810/.

[57] *Elgin Community Service Officer Charged with Theft of Explorer Funds*, Chicago Tribune (Jan. 4, 2016), *available at* http://www.chicagotribune.com/suburbs/elgin-courier-news/news/ct-ecn-elgin-police-criminal-charges-st-0105-20160104-story.html.

[58] Christopher N. Osher, *Denver Inmate Abuse Case Brings Up Old Questions about depty conduct*, Denver Post (Apr. 27, 2016), *available at* https://www.denverpost.com/2014/09/03/denver-inmate-abuse-case-brings-up-old-questions-about-deputy-conduct/.

[59] J. Heilemann et. al., *Uncle Sam Doesn't Want You*, 22 Wash. Monthly 38 (Dec. 1990).

"senior fisheries officer[s]."[60] Many of these government officials exercise only *de minimis* authority. Yet they are nonetheless considered "officers" in today's ordinary speech.

References to military officers comprise 28% of our overall sample. As at the Founding, there remains a distinction between "commissioned officers" and "non-commissioned officers" (NCOs). Today, commissioned officers—all 359,090 of them—have each received a presidential commission and confirmed by the Senate.[61] This includes even the most recent ROTC graduate.

By contrast, a non-commissioned officer or NCO is one who climbs to a particular rank among enlisted service members and exercises even modest authority over other enlisted service members.[62] Combined, the two classes of "officers" comprise more than 64.5% of the entire military.[63] And all of them—NCOs as well as commissioned officers—are considered "officers."

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[60] Carlos M. Duarte, *Will the Oceans Help Feed Humanity?*, 59 Bioscience 967 (2009).

[61] U.S. Dep't of Defense, *Officer Rank Insignias*, https://www.defense.gov/About/Insignias/Officers/; Dep't of Defense, 2016 Demographics Report 6 (2016).

[62] See U.S. Dep't of Defense, *Enlisted Rank Insignias*, https://www.defense.gov/About/Insignias/Enlisted/; see also Non-commissioned officer, Black's Law Dictionary 1258 (10th ed. 2014) ("An enlisted person in the Army, Air Force, or Marine Corps in certain pay grades above the lowest pay grade.").

[63] Dep't of Defense, 2016 Demographics Report 6, 15 (2016) (916,078 of 1,419,231; of those, 359,090 are commissioned and 546,988 are NCOs).

Our data also reveal that occasionally the public and private senses of the word "officer" are inverted. The corpus contains a handful of references to corporate employees outside the top brass being referred to as "officers"—i.e "security officer," "officer in the church," and "loan officer." More rare is when a government position is described using corporate jargon. For example, in 2009 President Obama created a position within the White House called the "Chief Technology Officer," tasked with "harness[ing] the power of technology, data, and innovation to advance the future of our Nation."[64] Interestingly enough, the White House did not consider the "Chief Technology Officer" an officer under the *Buckley* test until the position was codified in 2017 legislation.[65]

In light of these data, it is possible that the D.C. Circuit's understanding of the *Buckley* test has its origins in an erroneous—and almost certainly subconscious—importation of the *business* sense of the word "officer" to the Constitution. Contextually this makes little sense. Even today, the ordinary meaning of a government "officer" is much broader—extending to "archaeological preservation officers" and "animal control officers."

In short, our vernacular certainly considers an administrative law judge an "Officer of the United States." Our legal system should, too.

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[64] Office of Science and Technology Policy, *Office of the Chief Technology Officer*, https://obamawhitehouse.archives.gov/administration/eop/ostp/divisions/cto/.

[65] See American Innovation and Competiveness Act, Pub. L. No. 114-329, § 604, 130 Stat. 2969, 3037 (2017).

CONCLUSION

The D.C. Circuit's decision does not reflect either the original or modern sense of the phrase "Officers of the United States" which extends to any federal employee exercising non-negligible government authority. The Court should therefore reverse, and fashion an empirically sound test grounded in the linguistic meaning of the Constitution.

Respectfully submitted,

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APPENDIX

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No. 17-130

In The
Supreme Court of the United States

RAYMOND J. LUCIA AND
RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

**On Writ Of Certiorari To The
United States Court Of Appeals
For The District Of Columbia Circuit**

BRIEF OF SHOW, INC. AS *AMICUS CURIAE* SUPPORTING PETITIONERS

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INTEREST OF THE *AMICUS CURIAE*[1]

SHOW, Inc. is an affiliate of the Tennessee Walking Horse National Celebration, which annually sponsors the premier walking horse competition. To eliminate cheating in such events, in 1970, Congress passed the Horse Protection Act, 15 U.S.C. §§1821-1831. The Department of Agriculture administers the HPA, and certifies SHOW to license inspectors to examine horses for compliance with USDA regulations. USDA inspectors attend some events and also inspect horses for compliance. If an inspector is of the opinion a horse is non-compliant, management is informed, and the horse is disqualified.

The USDA can seek administrative penalties against persons it alleges violated the HPA. The HPA mandates:

> No civil penalty shall be assessed unless such person is given notice and an opportunity for a hearing before the Secretary with respect to such violations. The amount of such civil penalty shall be assessed by the Secretary by written order.

15 U.S.C. §1825(b)(1). USDA administrative law judges adjudicate enforcement proceedings, issuing an initial decision. Any party can appeal the ALJ's decision to

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[1] *Amicus* affirms that no counsel for a party authored this brief in whole or in part. No person other than *amicus*, its counsel and FAST (Foundation for the Advancement and Support of the Tennessee Walking Show Horse) made a monetary contribution to its preparation or submission. Counsel for the parties filed blanket consents to the filing of *amicus* briefs.

the USDA's Judicial Officer, a Senior Level employee to whom the Secretary has delegated the authority to make final decisions. 7 C.F.R. §2.35.

USDA ALJs, like SEC ALJs, exercise significant authority, but are not appointed as inferior officers by the Secretary. The Judicial Officer, who makes the final decision of the Department, is not appointed as a principal officer. No HPA civil penalty has ever been assessed by a lawfully appointed inferior officer or principal officer. SHOW has an interest in ensuring that the power to preside over and decide enforcement proceedings is vested in officials who are lawfully appointed.

SUMMARY OF ARGUMENT

The government concedes that SEC ALJs are inferior officers but does not address what caused the D.C. Circuit to reach a contrary conclusion. This case is before this Court because the D.C. Circuit wrongly interpreted *Freytag v. C.I.R.*, 501 U.S. 868 (1991) as holding that the Tax Court's special trial judges were inferior officers because they made final decisions that were not subject to review by a superior officer. The court then reviewed the statute and rules governing proceedings before SEC ALJs, and concluded the ALJ initial decisions were subject to discretionary review by the Commission before they became final. Lacking final decision making authority, SEC ALJs were employees, not officers.

The court did not review the relevant Tax Code provisions or Tax Court Rules that also provide that STJ decisions are subject to review by Tax Court judges. Further, since the Tax Court is a court of law, and not a part of the executive, STJ decisions are subject to discretionary review by judges on the courts of appeals, principal officers who serve in the same branch as STJs. Nor did the D.C. Circuit discuss the Appointments Clause decisions *Freytag* cited, which held that STJs were inferior officers, as opposed to principal officers, because STJ decisions were subject to review by Tax Court judges. *Freytag* did not hold that STJs made final decisions that were not subject to review by a superior officer. Finally, in brushing aside the petitioners' reliance on *Edmond v. U.S.*, 520 U.S. 651 (1997), the D.C. Circuit failed to recognize that if Tax Court STJs made final decisions that were not subject to review by any superior officer, then STJs would have to be appointed as principal officers.

This Court should reject the D.C. Circuit's holding that final-decision-making-authority is a necessary characteristic of judges who function as inferior officers, and reaffirm that judges who make final decisions that are not subject to review by a superior officer in the same branch must be appointed by the President with the advice and consent of the Senate.

ARGUMENT

I. CONFLICTING INTERPRETATIONS OF *FREYTAG*.

Freytag v. C.I.R. held that Tax Court special trial judges were inferior officers of the United States who were properly appointed by the Chief Judge of a court of law. When deciding whether FDIC ALJs were officers, in *Landry v. FDIC*, 204 F.3d 1125, 1132 (D.C. Cir. 2000), the D.C. Circuit found the "line between 'mere' employees and inferior officers anything but bright." The court considered *Freytag* "the most analogous case," but held that ALJs were distinguishable from STJs because the "authority of STJs [is] not matched by ALJs here." *Id.* at 1133. According to the D.C. Circuit, STJs had "the authority to render the *final* decision of the Tax Court in declaratory judgment proceedings and in certain small-amount tax cases," while the "ALJs here can never render the decision of the FDIC." *Id.* (emphasis in original). While acknowledging that "[i]t is, to be sure, uncertain just what role the STJs' power to make final decisions played in *Freytag*," the D.C. Circuit believed "the STJs' power of final decision in certain classes of cases was critical to the Court's decision." *Id.* at 1133, 1134.

In *Burgess v. FDIC*, 871 F.3d 297, 300 (5th Cir. 2017), in addressing whether FDIC ALJs were officers, the Fifth Circuit recognized that the *Landry* "court read *Freytag* as holding that a government worker must have final decision-making authority to be considered an Officer." The *Burgess* court concluded that

Freytag held that the STJs' significant duties brought them under the Appointments Clause and that "[t]he Court's additional statement – that these duties and discretion, coupled with the power to enter final judgments also makes the STJs Officers – was dicta or an alternative basis for its decision." *Id.* at 301.

In deciding whether SEC ALJs were officers, in *Lucia v. SEC*, 832 F.3d 277, 285 (D.C. Cir. 2016), the panel recognized "*Landry* is the law of the circuit," and concluded that since "no initial decision of its ALJs is independently final," SEC ALJs are not officers. *Id.* at 287. Moreover, the *Lucia* panel rejected the petitioners' reliance on *Edmond v. United States*, 520 U.S. 651 (1997), in contending that the ability to render a final decision characterized principal officers, stating that *Edmond* "had no occasion to address the differences between employees and Officers." *Id.* at 285.

By assuming that STJs were inferior officers because of their "ability to 'render a final decision on behalf of the United States,'" the D.C. Circuit's constitutional "analysis begins, and ends," with "whether Commission ALJs issue final decisions of the Commission." *Id.* The court ignored the contradiction in its own argument: if STJs made final decisions, then STJs would have to be appointed as principal officers, since the authority to make final decisions that are not subject to review by a superior officer is the defining feature of judges who are principal officers.

Bandimere v. SEC, 844 F.3d 1168, 1174, 1179 (10th Cir. 2016), held that "*Freytag* controls the result

of this case," and "SEC ALJs are inferior officers under the Appointments Clause." The court rejected the SEC's argument that "ALJs are not inferior officers because they cannot render final decisions." *Id.* at 1182. The *Bandimere* majority disagreed with *Landry*'s and *Lucia*'s interpretation of *Freytag* "that final decision-making power is dispositive. . . ." *Id.* at 1182. In addressing *Edmond*, the court stated that "the Supreme Court considered final decisionmaking power as relevant to the difference between principal and inferior officers, not the difference between an officer and an employee." *Id.* at 1184.

These conflicting decisions arise from the D.C. Circuit distinguishing FDIC and SEC ALJs from Tax Court STJs on the premise that the STJs make final decisions, while ALJs do not. This premise is not supported by the Tax Code, Tax Court Rules or Tax Court's procedures, which provide that STJ decisions in small tax, limited-tax and declaratory judgment cases are subject to discretionary review by Tax Court judges before the decisions are entered as decisions of the court.

II. STJ DECISIONS ARE SUBJECT TO REVIEW BY TAX COURT JUDGES.

The procedures of the Tax Court differ markedly from the procedures of administrative agencies. *Freytag* held that the Tax Court, for the purpose of the Appointments Clause, was a court of law, independent of the executive, and its Chief Judge was authorized to

appoint STJs. 501 U.S. at 891. The Tax Court, as a court of law, is not subject to the Administrative Procedures Act. 5 U.S.C. §551(1)(B). The FDIC and SEC are agencies subject to the Administrative Procedures Act, specifically the two-tier appeal provision in §557(b). The D.C. Circuit's failure to appreciate the procedures utilized by the Tax Court contributed to its mistaken assumption that STJs made final decisions not subject to review by Tax Court judges.

A. The FDIC and SEC Employ a Two-Tier Review Procedure.

The Administrative Procedures Act provides that an ALJ "who presides at the reception of the evidence . . . shall make the recommended decision or initial decision required by section 557 of this title. . . ." 5 U.S.C. §554(d). In FDIC proceedings, an ALJ will "issue a decision" recommending proposed findings and a proposed order, file it with the Executive Secretary, and serve the parties. Within 30 days, the respondent can file exceptions to the recommended decision, and the record will be "forwarded to the Board of Directors for final decision." *Landry*, 204 F.3d at 1128. The Board's decision is final for purposes of appeal to a court of appeals.

SEC ALJs render initial decisions. 5 U.S.C. §557(b). SEC rules require the record be certified to the Commission for discretionary review, either on the Commission's own initiative or if an appeal is filed. If Commission review is not timely sought, or the

Commission declines to exercise its discretionary right of review, the ALJ's decision will "be deemed the action of the Commission." *Lucia*, 832 F.3d at 281-82. Notice is then given by the Office of General Counsel "that the initial decision of the administrative law judge has become the final decision of the Commission" and "is hereby effective."[2] If a timely appeal to the Commission is filed, and review granted, the Commission's decision is final for purposes of appeal.

The two-tier appeal system, required by the APA, is the source of the current Appointments Clause controversy. The two-tier system creates an appearance that ALJs act independent from their employer, by denying the Department Head the authority to appoint or fire ALJs. Hence the problem: if the Department Head cannot appoint ALJs, and ALJs exercise the significant authority of an officer, then their appointment violates the Appointments Clause.

B. The Tax Court Abolished the Two-Tier Appeal Procedure.

Commencing in 1944, the Presiding Judge of the Tax Court could appoint an attorney from the legal staff to conduct "the hearing in accordance with the Court's rules of practice," who "shall prepare and submit to the Court or a Division thereof a report of his findings of fact . . . and copies thereof shall be served

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[2] *In the Matter of Neologic Animation, Inc.*, Admin. Proc. File No. 3-16595 (2015), which can be found on the SEC website at https://www.sec.gov/litigation/apdocuments/apclosed-fileno-asc.xml.

upon both parties."[3] Thereafter, the parties "may file exceptions thereto which will be considered by the Division to which the case is assigned."[4] Initially, the Tax Court operated under a two-tier appeal and review system.

In 1969, the Tax Court "established a small tax division under the supervision of a judge of the court."[5]

> The majority of the cases were assigned to STJs for hearing and the preparation of summary findings of fact and opinion. The report of the special trial judge is then submitted to the chief judge, or if the chief judge so directs, to a judge or division of the court for review.[6]

T.C. Rule 177 (1984) provided: "Neither briefs nor oral argument will be required in small tax cases." Small tax cases did not provide for taking exceptions or filing appeals to the Tax Court judges.

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[3] Tax Court Rule 48 (1944), found in the Brief for the Respondent, *Ballard v. C.I.R.*, 544 U.S. 40 (2005) (Nos. 03-184 and 03-1034), 2004 WL 2336550 at *6a-*7a (cited hereafter as "C.I.R. Brief at *___").

[4] *Id.*

[5] H. Dubroff & B. J. Hellwig, *The United States Tax Court: An Historical Analysis*, 828 (Government Publishing Office, 2d ed. 2014). The 1979 original edition resulted from the Tax Court granting Professor Dubroff permission to prepare a comprehensive history of the Court. The history was periodically updated in articles in the Albany Law Review. In 2010, the Court concluded that a comprehensive update should be prepared, resulting in the 2014 second edition. *Id.* at Preface, pages i-iv.

[6] *Id.* at 829.

In 1976, the Tax Court exempted declaratory judgment and limited-amount tax cases from the objection and appeal procedure, making them like small tax cases.[7] The purpose was "to make changes in the present practices of the Court in order to dispose of pending cases more promptly and efficiently."[8] When the two-tier appeal procedure was eliminated for limited-amount cases, the Chief Judge issued United States Tax Court General Order No. 5, at 1 (1976), requiring that:

> As soon as practicable after hearing a case assigned to him in accordance with this order, a Special Trial Judge shall prepare his proposed findings of fact and opinion and submit them to the Chief Judge, or another Judge designated by him for that purpose. The proposed findings of fact and opinion of the Special Trial Judge shall not constitute the findings of fact and opinion of the Court unless reviewed and adopted by the Judge to whom the case is assigned, and the report is approved by the Chief Judge.[9]

In 1983, the Tax Court amended Rule 182, replacing it with Rule 183 (1984), governing a STJ's report in cases assigned under §7443A(b)(4). The STJ's decision would no longer be filed and served on the parties; it was submitted to the Chief Judge. As a result, by

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[7] C.I.R. Brief, *supra* n. 3, at *36.

[8] *Id.* at *8a.

[9] *Id.* at *8a-*10a.

1983, "the procedures for service of the reports of special trial judges were completely eliminated."[10]

The elimination to the two-tier exception and appeal procedure was noted in *Freytag*. In *Freytag v. C.I.R.*, 904 F.2d 1011, 1015, n. 8 (5th Cir. 1990), the court observed that previously "litigants were furnished with a copy of the special trial judge's proposed opinion and filed exceptions thereto," but "litigants are no longer afforded this opportunity, [and] this change in rules, in our view, confirms that the Tax Court's relationship with its special trial judges cannot be analogized to typical appellate review." This Court's decision in *Freytag* noted that the Chief Judge received the STJ's report on October 21, 1987, and adopted it that same day. 501 U.S. at 872, n. 2. While acknowledging that the "Chief Judge had a duty to review the work of the Special Trial Judge," the Court pointed out that the STJ had submitted a report to the Chief Judge four months before, thus, "the chronology does not appear to us to be at all significant." *Id.*

C. The Tax Court Employs a Deliberative Procedure.

In place of the two-tier appeal procedure, the Tax Court employed a deliberative procedure under which the Tax Court judges reviewed reports of judges and STJs before they were entered as decisions of the court.

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[10] H. Dubroff and C. Greene, *Recent Developments in the Business and Procedures of the United States Tax Court*, 52 Albany L. Rev. 33, 64 (1987).

In cases assigned under §7443A(b)(1)-(3), STJs' proposed decisions are not final independent of review by Tax Court's judges. The STJs' authority is limited by the Tax Court "Rules and such directions as may be prescribed by the Chief Judge." T.C. Rule 180 (1984). STJs are "[s]ubject to the specifications and limitations in the order designating a Special Trial Judge and in accordance with the applicable provisions of these Rules." T.C. Rule 181 (1984). Congress authorized the Tax Court judges to supervise STJs who would make the decision of the court by making the STJs "subject to such conditions and review as the court may provide." I.R.C. §7443A(c) (1986).

The Tax Court's supervision of STJ decision-making is driven by the goal to speak with one voice in the court's decisions. Since 1927, the Tax Court has employed a conference procedure to review the judges' reports.[11] The conference review "process has been shaped by the court's desire to provide an impartial and expedient judicial review of tax controversies that will serve as a source of uniform precedents for the Service and the public."[12] Under the conference procedure, a judge's findings of fact and opinion in a case are included in a report that is submitted to the Chief Judge.

In 1982, except in declaratory judgment cases, Congress provided the report could be stated orally in the transcript as a bench opinion if the judge was "satisfied as to the factual conclusions to be reached in the

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[11] Dubroff, n. 5 at 735, n. 62.

[12] *Id.* at 729.

case and that the law to be applied thereto is clear."[13] Bench opinions are transcribed, and the Chief Judge "requested that the transcript of cases in which bench opinions were rendered be forwarded to him, or in small tax cases, to the judge in charge of the small tax division."[14] I.R.C. §7459(a) and (b) (1982) ("The decision shall be made by a judge in accordance with the report of the Tax Court, and such decision so made shall, when entered, be the decision of the Tax Court.").

Uniformity in Tax Court decisions is accomplished because:

> The report (opinion or memorandum opinion) is transmitted to the chief judge who, with the assistance of the legal staff, reviews the opinion, notes any comments or suggested revisions, and decides whether to direct that the opinion be reviewed by the Court Conference. Summary opinions authored by special trial judges undergo a similar review by a Presidentially appointed judge assigned to the Small Tax Case Division.[15]

This Court observed in *Ballard* that the Tax Court operated under "a novel practice regarding the report the special trial judge submits post-trial to the Chief Judge." 544 U.S. at 56. In *Ballard*, the Commissioner defended this deliberative procedure,[16] arguing there

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[13] *Id.* at 740.

[14] *Id.* at 749.

[15] *Id.* at 735.

[16] C.I.R. Brief, *supra*, n. 3, at *8.

is no legal prohibition against judges exchanging ideas.[17] Where multiple judges participate in making the decision, that decision is not final until it is released, and "nothing precludes such interchange between the STJ and a Tax Court judge."[18]

D. The Tax Code, Tax Court Rules and Orders Authorize Tax Court Judges to Review STJ Decisions Prior to their Entry as the Decision of the Court.

In cases the Chief Judge assigns to STJs under §7443A(b)(1)-(4), the Tax Code, Tax Court Rules and Orders make STJ decisions subject to review by Tax Court judges prior to their being entered as decisions of the court.

1. STJ declaratory judgment decisions are subject to review.

I.R.C. §7443A(b)(1) (1984) authorizes the Chief Judge to assign "any declaratory judgement proceeding" to an STJ and §7443A(c) provides that the "court may authorize a special trial judge to make the decision of the court . . . subject to such conditions and review as the court may provide." T.C. Rule 180 (1984) required that the STJ's adjudicative activities be "in accordance with these Rules and such direction as may be prescribed by the Chief Judge." T.C. Rule 181 (1984)

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[17] *Id.* at *20.

[18] *Id.* at *21.

made the STJ's powers and duties "[s]ubject to the specifications and limitations in the order . . . and in accordance with the applicable provisions of these Rules. . . ."

Decisions in declaratory judgment cases would "ordinarily be made on the basis of the administrative record" compiled before the Internal Revenue Service. T.C. Rule 217(a) (1984). T.C. Rule 152, authorizing bench opinions, did not apply to declaratory judgment cases. T.C. Rule 218(a) (1984) provided that in declaratory judgment cases, where the STJ

> is authorized in the order of assignment to make the decision, the opinion of the Special Trial Judge and his proposed decision shall be submitted to and approved by the Chief Judge or by another Judge designated by the Chief Judge for that purpose, prior to service of the opinion and decision upon the parties.

The STJ's proposed decision in a declaratory judgment case is subject to review by the Chief Judge, or a designated judge, and "frequent consultation between judges is the rule, rather than the exception."[19] Only after the proposed decision was submitted to the Chief Judge would the STJ's decision become the decision of the court.

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[19] Dubroff, *supra* n. 5 at 759.

2. STJ decisions in small tax cases are subject to review.

When *Freytag* was decided, small tax cases involved disputes under $10,000 where the taxpayer elected to proceed under the informal procedures authorized by I.R.C. §7463 (1984) and T.C. Rules 170-179 (1984). I.R.C. §7443A(b)(2) (1984) authorized the Chief Judge to assign small tax cases to an STJ, who would preside over the case "in accordance with these Rules and such direction as may be prescribed by the Chief Judge." T.C. Rule 180 (1984). I.R.C. §7443A(c) (1984) provided that the "court may authorize a special trial judge to make a decision of the court" in a small tax case "subject to such conditions and review as the court may provide."

Unless a bench opinion had already been dictated into the transcript, T.C. Rule 182(a) (1984) required that the STJ

> who conducts the trial of a small tax case, shall, as soon after such trial as shall be practicable, prepare a summary of the facts and reasons for his proposed disposition of the case, which shall then be submitted promptly to the Chief Judge, or, if the Chief Judge shall so direct, to a Judge or Division of the Court.

In small tax cases, STJ decisions were subject to discretionary review before they were entered as the decision of the court and were "subject to such conditions and review as the Chief Judge may provide." T.C. Rule 182(c) (1984). STJs, even in small tax cases

assigned under §7443A(b)(2), were subject to supervision by Tax Court judges appointed as principal officers, and the STJs' proposed decisions were "subject to such conditions and review as the court may provide." I.R.C. §7443A(c).

3. STJ decisions in limited-amount cases are subject to review.

In a limited-amount case, not exceeding $10,000, where the taxpayer did not elect to proceed as a small tax case, I.R.C. §7443A(b)(3) permitted the Chief Judge to assign the case to an STJ, who would preside over the case "in accordance with Rules and such direction as may be prescribed by the Chief Judge." T.C. Rule 180 (1984). I.R.C. §7443A(c) (1984) provided that the "court may authorize a special trial judge to make a decision of the court" in a limited-amount tax case "subject to such conditions and review as the court may provide."

Unless a bench opinion had already been dictated into the transcript, T.C. Rule 182(b) (1984) required that

> a Special Trial Judge who conducts the trial of a case (other than a small tax case) where neither the amount of the deficiency placed in dispute (within the meaning of Code Section 7463), nor the amount of any claimed overpayments, exceeds $10,000 shall, as soon after such trial as shall be practicable, prepare proposed findings of fact and opinion, which shall then be submitted promptly to the Chief Judge.

The Chief Judge, in a 1976 Order, required that:

> The proposed findings of fact and opinion of the Special Trial Judge shall not constitute the findings of fact and opinion of the Court unless reviewed by the Judge to whom the case is assigned, and the report is approved by the Chief Judge.[20]

STJs, even in limited-amount tax cases assigned under §7443A(b)(3), are subject to supervision by Tax Court judges appointed as principal officers.

4. STJ decisions in "any other proceeding" are subject to review.

I.R.C. §7443A(b)(4) authorized the Chief Judge to assign "any other proceeding" to a STJ, but §7443A(c) did not authorize the STJ to "make the decision of the court." T.C. Rule 183 (1984) provided that after the trial, and all briefs had been submitted, "the Special Trial Judge shall submit his report, including his findings of fact and opinion, to the Chief Judge, and the Chief Judge will assign the case to a Division of the Court." The report was not filed or served, so there was no two-tier appeal procedure. The judge to whom the case was referred could adopt, modify or reject the report, while giving due regard to the STJ's findings of fact, which were presumed correct. T.C. Rule 183(c) (1984).

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[20] C.I.R. Brief, *supra* n. 3 at *10a.

In *Ballard*, this Court decided that Tax Court Rule 183 required that the STJ's report be a part of the court's records in cases assigned under §7443A(b)(4). To address the *Ballard* decision, in 2005, Tax Court Rule 183 was amended, requiring the STJ's report be filed and served, giving the parties an opportunity to file objections. However, the Tax Court's Rules in effect in 1990, and today, governing small tax, limited-amount and declaratory judgment cases, were not changed, and the STJ's proposed decision becomes the decision of the court under the collaborative-decision system the Commissioner described and defended in *Ballard*. Consequently, no STJ's proposed decision ever becomes the decision of the court independent of review by a Tax Court judge.

III. STJ DECISIONS ARE SUBJECT TO REVIEW BY JUDGES IN SUPERIOR COURTS OF LAW.

In *Freytag*, the divisive issue was not whether STJs were employees or officers, but whether the Tax Court was a court of law or part of the executive. This Court held the Tax Court was an Article I court that "exercises judicial, rather than executive, legislative, or administrative power" and "remains independent of the Executive and Legislative Branches." 501 U.S. at 890-91. Four Justices, while concurring in the judgment, contended the Tax Court was in the executive, because if the Tax Court was a court of law, this raised a separation of powers issue since the President could remove a judge for cause.

The separation of powers issue arose in *Kuretski v. C.I.R.*, 755 F.3d 929 (D.C. Cir. 2014), *cert. denied*, 135 S. Ct. 2309 (2015). The D.C. Circuit rejected *Freytag*'s holding that the Tax Court was a court of law, deciding that it was an Article I court within the executive branch. In response, in 2015, Congress amended I.R.C. §7441 to reflect that "[t]he Tax Court is not an agency of, and shall be independent of, the executive branch of the Government."

Battat v. C.I.R., 148 T.C. No. 2 (2017), reaffirmed the Tax Court's status as a court of law, pointing out that Tax Court judges exercise judicial power to the exclusion of any other function and resemble federal district courts whose judgments are appealable only to regional U.S. courts of appeals and are reviewable under the standards of district court bench trials as opposed to review of agencies' decisions under APA §706(2)(A). Special trial judges resemble magistrate judges. *See Battat*, 148 T.C. No. 2 at 1-11.

STJs' decisions, when entered as decisions of the court, are final decisions of a court of law for purposes of appeal, and, unless an appeal is waived, are reviewable by judges of United States courts of appeals. I.R.C. §7481. Because the Tax Court is a court of law, there is a second level of discretionary review of STJ decisions by principal officers in the same branch. In small tax cases, filed under §7463 and T.C. Rules 170-178, the taxpayer waives the right to appeal to an Article III court. *See Cole v. C.I.R.*, 958 F.2d 288, 289 (9th Cir. 1992). In limited-amount cases, the decision of the STJ, when entered, is the decision of the court for purposes

of appeal. *See Crawford v. C.I.R.*, 266 F.3d 1120, 1123 (9th Cir. 2001). STJ declaratory judgment decisions are reviewable in United States courts of appeals. I.R.C. §7481(a)(1), *Carter v. C.I.R.*, 746 F.3d 318, 321 (7th Cir. 2014).

Tax Court STJs are officers, not employees, because they exercise significant authority. They are inferior officers because their decisions are subject to review by Tax Court judges and courts of appeals judges, superior principal officers in the same branch.

IV. *FREYTAG* DOES NOT HOLD THAT STJS MAKE DECISIONS INDEPENDENT OF DISCRETIONARY REVIEW BY TAX COURT JUDGES.

In *Freytag*, the C.I.R. conceded that STJs were inferior officers in three types of cases because they could "render the decisions of the Tax Court." 501 U.S. at 882. The authority to render the decision of the court means that the STJ decision is final for purposes of appeal to an Article III court, not that the decision was unreviewable by a Tax Court judge. I.R.C. §7481. The authority to make the "decision of the court" does not equate with the authority to make a decision that is not subject to review by a principal officer. This was the conclusion in the two cases this Court cited in *Freytag*, which held that because of their significant authority, STJs were officers as opposed to employees, but were inferior officers, as opposed to principal officers,

because the STJs' decisions were subject to review by Tax Court judges.

Freytag, filed in March 1982, was one of nine consolidated test cases arising from a tax shelter scheme promoted by First Western and Samuels, Kramer. The test cases were initially assigned to Tax Court judge Wilbur. Trial commenced in 1984, but, when Judge Wilbur became ill, the cases were assigned to STJ Powell to "preside over the trial as an evidentiary referee." 501 U.S. at 871. After Judge Wilbur retired, the Chief Judge assigned the cases to STJ Powell for "preparation of written findings and an opinion." *Id.* STJ Powell submitted his "proposed findings and opinion" on October 21, 1987, which the Chief Judge promptly adopted as the decision of the court. *Id.* at 872, n. 2.

"Pursuant to section 7443A and Rules 180, 181 and 182," the petitions in *First Western Govt. Securities, Inc. v. Commissioner*, 94 T.C. 549, 552 (1990) and *Samuels, Kramer & Co. v. Commissioner*, 930 F.2d 975 (2d Cir. 1991), *cert. denied*, 502 U.S. 957 (1991), were also assigned to STJ Powell. After the test-cases decision, but before their cases were tried, the petitioners filed motions to vacate the assignment, requesting their cases be "assigned to a Presidentially appointed Tax Court judge." *First Western*, 94 T.C. at 549.

In response, the C.I.R. contended that since an STJ assigned under §7443A(b)(4) could not make the decision of the court, the STJ functioned as an employee, not an officer. The Tax Court rejected this position, concluding that because STJs "may be assigned

any case and may enter decisions in certain cases, it follows that special trial judges exercise significant authority" and "are officers, not employees of the United States." *Id.* at 557.

The Tax Court then addressed whether STJs were inferior or principal officers. Relying on *Morrison v. Olsen*, 487 U.S. 654 (1988), the court acknowledged the "line between inferior and principal officer is one that is far from clear," but concluded STJs were inferior officers, "[c]onsidering the limitations placed on the duties, jurisdiction and tenure of special trial judges." *Id.* at 558-59. Among those limitations, "[t]he chief judge of the Tax Court, a principal officer, has the authority to appoint and remove special trial judges without restriction" and "[t]he duties of special trial judges are defined and limited by the Order issued by the chief judge assigning a case to a special trial judge." *First Western*, 94 T.C. at 558 (citing Tax Court Rules 180, 181, 182 and 183).

In *Samuels, Kramer*, an interim appeal of the Tax Court's *First Western* decision, the Second Circuit first disposed of the taxpayer's argument that the STJ functioned as a principal officer. STJs were not principal officers, because "[s]pecial trial judges can be removed at any time by the Chief Judge" and the "Chief Judge also has absolute control over the extent of the duties that are assigned to special trial judges." *Id.* at 985. In rejecting the C.I.R.'s argument that an STJ assigned under §7443A(b)(4) was not an officer because the STJ could not make the decision of the court, the court held that although "the ultimate decisional authority in

cases under section 7443A(b)(4) rests with the Tax Court judges, the special trial judges do exercise a great deal of authority in such cases" and STJs are "more than mere aids to the judges of the Tax Court." *Id.* at 985-86.

In *First Western* and *Samuels, Kramer*, the courts recognized that all cases assigned to STJs were subject to review by Tax Court judges. This is required by I.R.C. §7443A(a) and (c), under which STJs are appointed by and serve at the discretion of the Chief Judge who "may authorize" the STJ to "make the decision of the court . . . subject to such conditions and review as the court may provide." The D.C. Circuit, in *Landry* and *Lucia*, did not discuss the "conditions and review" STJ decisions were subject to in declaratory judgment, small tax and limited-amount cases.

V. JUDGES WHO MAKE FINAL DECISIONS FUNCTION AS PRINCIPAL OFFICERS.

If STJs' decisions are independent of discretionary review by a principal officer, as *Landry* and *Lucia* assume, then, under this Court's post-*Freytag* Appointments Clause decisions involving judges, STJs would have to be appointed as principal officers. If *Landry* and *Lucia* are correct, then *Freytag*'s holding that STJs are inferior officers is incorrect.

Weiss v. U.S., 510 U.S. 163, 170 (1994), upheld the appointment of the judges on the Navy-Marine Corps Court of Military Review because each of the military judges had been appointed as a commissioned officer

by the President. Justice Souter concurred, with the understanding that the judges were inferior officers "because not only the legal rulings of military judges but also their fact finding and sentencing are subject to *de novo* scrutiny by the Courts of Military Review." *Id.* at 193.

The petitioners, in *Ryder v. U.S.*, 515 U.S. 177 (1995), complained that two civilian judges' appointments on the United States Coast Guard Court of Military Review by a General Counsel contravened the Appointments Clause requirement that officers be appointed by the Department Head. This Court agreed, concluding that "one who makes a timely challenge to the constitutional validity of the appointment of an officer who adjudicates his case is entitled to a decision on the merits of the question and whatever relief may be appropriate if a violation occurred." *Id.* at 182-83.

In *Edmond v. U.S.*, 520 U.S. 651 (1997), the Secretary of Transportation had appointed the two civilian judges on the renamed Coast Guard Court of Criminal Appeals. The petitioner contended the judges held "principal-officer status" because of "the importance of the responsibilities that Court of Appeals judges bear." *Id.* at 662. Citing *Freytag*, this Court noted "[t]his, however, is also true of offices that we have held 'inferior' within the meaning of the Appointments Clause," thus, the "exercise of 'significant authority pursuant to the laws of the United States' marks, not the line between principal and inferior officer for Appointments Clause purposes, but rather, as we said in *Buckley*, the line between officer and nonofficer." *Id.*

The Court announced a "definitive test" for determining whether a judge functions as an inferior or principal officer:

> Whether one is an "inferior" officer depends on whether he has a superior. It is not enough that other officers may be identified who formally hold a higher rank, or possess responsibilities of a greater magnitude. If that were the intention, the Constitution might have used the phrase "lesser officer." Rather, in the context of a Clause designed to preserve political accountability relative to important Government assignments, we think it evident that "inferior officers" are officers whose work is directed and supervised at some level by others who are appointed by Presidential nomination with the advice and consent of the Senate.

Id. at 662-63. The judges in *Edmond* were officers because of the significance of their authority. They were inferior officers because their decisions were subject to discretionary review by judges with the power to reverse those decisions, who were principal officers on Court of Appeals for the Armed Forces, a court in the Department of Defense, and, like the Department of Transportation, in the executive branch. The judges in *Edmond* were inferior officers because "[w]hat is significant is that the judges of the Court of Criminal Appeals have no power to render a final decision on behalf of the United States unless permitted to do so by other Executive officers." *Id.* at 664.

Like the judges in *Edmond*, STJs are officers because of the significant authority they exercise. STJs are inferior officers, as distinguished from principal officers; they have no power to render a final decision on behalf of the United States unless permitted to do so by judges in courts of law who are principal officers.

CONCLUSION

In its Brief for Respondent, at page 14, the government describes *Freytag* as holding that STJs are inferior officers since "special trial judges are also authorized by law to 'render the decisions of the Tax Court [i.e., final decisions] in declaratory judgment proceedings and limited-amount tax cases.'" There would be no need to insert "[final decision]" in the quote if this Court had said "final decision," which it did not. *Freytag* did not hold STJs make final decisions, if, by that, one means decisions that are independent of review by a superior principal officer.

The Brief for Respondent, at pages 10-11, states: "Upon further consideration, and in light of the implications for the exercise of executive power under Article II, the government is now of the view that such ALJs are officers given that they exercise 'significant authority pursuant to the laws of the United States.'" The government suggests that the question of ALJs' status "is also extremely important because it affects . . . the conduct of adversarial administrative proceedings in other agencies within the government," *id.* at

10, specifically identifying the Department of Agriculture, *id.* at 26. This Court's decision will be relevant to the interest of this *amicus*, since in USDA administrative proceedings, not only is the status of ALJs important, so is the status of the Judicial Officer, a Senior Level employee whose decisions are not subject to review by a principal officer in the executive branch.

This Court should remedy the confusion caused by *Landry* and *Lucia* by following *Freytag* and *Edmond*. SEC ALJs are officers because of the significant authority they exercise, and they are inferior officers because their work is directed and supervised by duly appointed principal officers in the same branch.

Respectfully submitted,

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February 2018

No. 17-130

In The Supreme Court of the United States

RAYMOND J. LUCIA AND
RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

BRIEF OF *AMICI CURIAE* STATES OF UTAH, ALABAMA, ARKANSAS, INDIANA, KANSAS, LOUISIANA, MICHIGAN, MISSOURI, NEBRASKA, OKLAHOMA, RHODE ISLAND, SOUTH CAROLINA, TEXAS, WISCONSIN, AND WYOMING SUPPORTING PETITIONERS

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QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are Officers of the United States within the meaning of the Appointments Clause.

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INTEREST OF *AMICI CURIAE*[1]

Amici are the States of Utah, Alabama, Arkansas, Indiana, Kansas, Louisiana, Michigan, Missouri, Nebraska, Oklahoma, Rhode Island, South Carolina, Texas, Wisconsin, and Wyoming. They want to protect the structural safeguards embedded in the Constitution that allow the States and the federal government to "controul each other." The Federalist No. 51, at 351 (James Madison) (J. Cooke ed. 1961). The Appointments Clause ranks among the most significant of those safeguards. *Amici* seek a ruling from this Court that preserves their ability to use the Clause for that purpose.

SUMMARY OF ARGUMENT

In our constitutional drama, the States are not Fredo Corleone, sniveling in a boathouse to a later-born entity and demanding respect. *See* The Godfather: Part II (Paramount Pictures 1974). Rather, "under our federal system, the States possess sovereignty concurrent with that of the Federal Government, subject only to limitations imposed by the Supremacy Clause." *Tafflin v. Levitt*, 493 U.S. 455, 458 (1990).

The Framers designed the Constitution to intentionally preserve State sovereignty. They planned on dual sovereigns becoming dueling sovereigns that would check each other's overreach. States' efforts to check federal excesses bear significant weight when

[1] The State of Utah, as *amicus curiae*, may file this brief without the parties' consent. Sup. Ct. R. 37.4.

they hold the federal government to account for disregarding the Constitution's structural safeguards.

The Appointments Clause is a critical structural safeguard. By circumscribing who may appoint principal and inferior federal officers, the Clause facilitates State efforts to hold the President and members of Congress politically accountable for good and bad appointments. The importance of those efforts cannot be overstated in an era when federal appointees can bring the weight of federal authority to bear on untold aspects of a concurrent sovereign's activities.

In resolving this case, the Court should emphasize the federal government's duty to ensure that its inferior officers take their stations in accordance with the Appointments Clause's mandates. Such a ruling will strengthen the States' efforts to discharge their sovereign duty of checking federal overreach for the people's benefit.

ARGUMENT

Like the Tenth Circuit, *Bandimere v. SEC*, 844 F.3d 1168, 1170 (10th Cir. 2016), Petitioners get it right: The Securities and Exchange Commission's administrative law judges are inferior officers. Those ALJs hold offices provided by law and exercise significant federal authority in a host of ways – some with career-ending consequences – when they adjudicate citizens' rights in adversarial proceedings. *See* Pet'rs' Br. 20-26. Those ALJs thus must accede to their offices

consonantly with the Appointments Clause, U.S. Const. art. II, § 2, cl. 2; *see Freytag v. Comm'r*, 501 U.S. 868 (1991); *Buckley v. Valeo*, 424 U.S. 1, 126 (1976) (per curiam). Here, everyone agrees that they did not do so. Pet'rs' Br. 15. That suffices to reverse the Court of Appeals' judgment.

Amici endorse Petitioners' arguments in support of reversal but will not belabor them. Instead, *amici* explain why arguments uniquely theirs to make also support the outcome Petitioners seek.

Those arguments arise from a lesson "every schoolchild learns" – that "our Constitution establishes a system of dual sovereignty between the States and the Federal Government." *Gregory v. Ashcroft*, 501 U.S. 452, 457 (1991). The Founders' constitutional design makes State sovereignty a bulwark against unlawful federal action. Allowing inferior officers to exercise federal power when they have not lawfully acceded to their offices erodes that unique (and uniquely important) bulwark.

I. The Founders Intended The Sovereign States To Check Federal Overreach.

A. Our Constitution Preserves State Sovereignty.

1. The Founders' ingenuity created "'a legal system unprecedented in form and design, establishing two orders of government.'" *Printz v. United States*, 521 U.S. 898, 920 (1997) (quoting *U.S. Term Limits, Inc.*

v. Thornton, 514 U.S. 779, 838 (1995) (Kennedy, J., concurring)). The Constitution not only created the federal government but kept the several States intact because "[p]reservation of the States as independent political entities" was "the price of union." *Id.* at 919. In fact, for almost 150 years, this Court's cases have recognized the Constitution's paramount concern for State sovereignty: "the preservation of the States, and the maintenance of their governments, are as much within the design and care of the Constitution as the preservation of the Union and the maintenance of the National government." *Texas v. White*, 74 U.S. (7 Wall.) 700, 725 (1868), *overruled in part on other grounds*, *Morgan v. United States*, 113 U.S. 476, 496 (1885).

By allocating power in a way that "preserves the integrity, dignity, and residual sovereignty of the States," the Constitution "ensure[s] that States function as political entities in their own right." *Bond v. United States*, 564 U.S. 211, 221 (2011). States reap the benefits – and bear the burdens – of "represent[ing] and remain[ing] accountable to [their] own citizens," *Printz*, 521 U.S. at 920, when they exercise the "numerous and indefinite" powers that the Constitution "reserve[s] to" them, The Federalist No. 45, at 313 (James Madison). Those powers operate on subjects closest to the people – their "lives, liberties, and properties," and "the internal order, improvement, and prosperity of the State." *Id.*

The Founders separated sovereignty that way to benefit the people. "The federal structure allows local policies 'more sensitive to the diverse needs of a

heterogeneous society,' permits 'innovation and experimentation,' enables greater citizen 'involvement in democratic processes,' and makes government 'more responsive by putting the States in competition for a mobile citizenry.' " *Bond*, 564 U.S. at 221 (quoting *Gregory*, 501 U.S. at 458). States can "respond, through the enactment of positive law, to the initiative of those who seek a voice in shaping the destiny of their own times without having to rely solely upon the political processes that control a remote central power." *Id.*

2. The Founders who split sovereignty's atom expected the States to check federal overreach. "[A]ction that exceeds the National Government's enumerated powers undermines the sovereign interests of States," *id.* at 225, entities with the institutional motive and ability to push back. Hence our constitutional design yields "a healthy balance of power between the States and the Federal Government" intended to "reduce the risk of tyranny and abuse from either front." *Gregory*, 501 U.S. at 458. As Madison put it, dual sovereignty creates a "double security" for "the rights of the people": "[t]he different governments will controul each other; at the same time that each will be controulled by itself." The Federalist No. 51, at 351.

But that outcome isn't guaranteed simply because the Constitution created separate governments. Achieving federalism's promise of "double security" requires "a proper balance between the States and the Federal Government." *Gregory*, 501 U.S. at 459. Dual sovereigns "will act as mutual restraints only if both are credible." *Id.*

3. State efforts to check federal overreach carry significant credibility when they rely on "the shape of the constitutional scheme." *Garcia v. San Antonio Metro. Transit Auth.*, 469 U.S. 528, 550 (1985). That's because "[a]part from the limitation on federal authority inherent in the delegated nature of Congress' Article I powers, the principal means chosen by the Framers to ensure the role of the States in the federal system lies in the structure of the Federal Government itself." *Id.*

Two parts of that structure warrant discussion here. First, States play a unique role (through the electoral college) in electing the President. U.S. Const. art. II, § 1, cl. 2-3. Second, the Founders intended the Senate to protect the States' interests. In that body, "each State received equal representation and each Senator was to be selected by the legislature of his State." *Garcia*, 469 U.S. at 551 (citing U.S. Const. art. I, § 3). To be sure, States no longer directly elect United States Senators, *see* U.S. Const. amend. XVII, but States still have "equal representation in the Senate," a structural feature whose importance "is underscored by the prohibition of any constitutional amendment divesting a State of equal representation without the State's consent." *Garcia*, 469 U.S. at 551 (citing U.S. Const. art. V.).

The historical record confirms that the Framers thought the Senate well suited to protecting the States. James Madison in "particular reli[ed] on the equal representation of the States in the Senate, which he saw as 'at once a constitutional recognition of the portion of sovereignty remaining in the individual States, and an

instrument for preserving that residuary sovereignty.'" *Id.* (quoting The Federalist No. 62, p. 408 (B. Wright ed. 1961)). Madison further reasoned "that 'the residuary sovereignty of the States [is] implied *and secured* by that principle of representation in one branch of the [federal] legislature.'" *Id.* (quoting The Federalist No. 43, p. 315 (B. Wright ed. 1961)).

In short, the Founders placed "procedural safeguards . . . in the structure of the federal system" to help "properly protect" the "State[s'] sovereign interests." *Id.* The Presidency and the Senate embody and superintend those safeguards.

B. The Appointments Clause Is A Structural Safeguard That Serves States' Sovereign Interests.

1. The Appointments Clause is a paradigmatic structural safeguard for checking federal overreach and protecting State sovereignty. It vests the President with power to "nominate, and by and with the Advice and Consent of the Senate," to appoint ambassadors, Justices of this Court, and other "Officers of the United States" whose offices are "established by Law." U.S. Const. art. II, § 2, cl. 2. It creates a different mechanism, however, for appointing "inferior Officers": As Congress "think[s] proper," it "may by Law vest the[ir] Appointment . . . in the President alone, in the Courts of Law, or in the Heads of Departments." *Id.*

The Founders designed the Appointments Clause to "prevent[] the diffusion of the appointment power."

Freytag, 501 U.S. at 878. This safeguard serves that purpose for at least three reasons.

First, one of the Founders' "greatest grievances against executive power" was the "manipulation of official appointments." *Id.* at 883 (internal quotation marks omitted). To them, the appointment power represented both "the most insidious and powerful weapon of eighteenth century despotism," *id.* (internal quotation marks omitted), and a means for "subvert[ing] democratic government," *id.* at 885. The Appointments Clause "addressed these concerns" by carefully delineating who could wield that power. *Id.* at 883.

Second, cabining the appointment power would "ensure that those who wielded it were accountable to political force and the will of the people." *Id.* at 884; *see also Edmond v. United States*, 520 U.S. 651, 663 (1997) (the "Clause [is] designed to preserve political accountability relative to important Government assignments"). "By requiring the joint participation of the President and the Senate" to appoint principal officers, the Clause allows the public to ascribe credit (or blame) for good (or bad) appointments to the responsible political actor(s). *Edmond*, 520 U.S. at 660. So too for the appointment of inferior officers, since their "work is directed and supervised at some level by others who were appointed by Presidential nomination with the advice and consent of the Senate." *Id.* at 663.

Third, the Framers thought that the Clause gave the Country the best chance at "a higher quality of

appointments." *Id.* at 659. They expected "that the President would be less vulnerable to interest-group pressure and personal favoritism than would a collective body." *Id.* In Hamilton's words, "[t]he sole and undivided responsibility of one man will naturally beget a livelier sense of duty and a more exact regard to reputation." The Federalist No. 76, at 510-11.

2. The concerns that motivated the Clause's adoption persist. States share them.

First, the federal government is omnipresent today in ways the Founders could not have contemplated. Like private parties, States feel "the inexorable presence of the administrative state," *Freytag*, 501 U.S. at 885, and can be subject to federal courts' judgments, *see, e.g.*, *Fitzpatrick v. Bitzer*, 427 U.S. 445, 453-57 (1976) (holding that Congress has power under Section 5 of the Fourteenth Amendment to abrogate State sovereign immunity). States thus share the Founders' interest in ensuring that federal officers do not become "despot[s]" who "subvert[ ]" their democratic governments when exercising federal power. *Freytag*, 501 U.S. at 883, 885 (internal quotation marks omitted). The Appointments Clause's strictures give States tools to help prevent those outcomes.

States use those tools by deploying their "political force," *id.* at 884, to seek "political accountability relative to important [federal] Government assignments," *Edmond*, 520 U.S. at 663. State officials interact frequently with the State's members of Congress and occasionally with the President or members of his

cabinet. When federal officers are appointed in accordance with the Appointments Clause's requirements, State officials can meaningfully call Executive and Legislative Branch officials to account for their appointees' acts.

Or State officials could use those interactions to suggest persons to be nominated as federal officers, thereby furthering the Clause's third purpose. Given the dual sovereigns' symbiotic relationship, *see Bond*, 564 U.S. at 220-22; 225, States need – and want – the federal government to succeed. Higher-quality nominees (and officers) should produce higher-quality outcomes for the Nation, the States, and the people. But State officials' best chances for proposing quality nominees exist only when it is clear (as the Appointments Clause requires) who makes the appointment. If, for example, a State had an interest in proposing a nominee to be an SEC ALJ, that State would not have known where to turn before this case arose. *See* Pet'rs' Br. 15 (noting that "[f]or years, no one (including government counsel) seemed to know how SEC ALJs were selected" – a secret disclosed only "in response to a discovery order from a federal judge" in this case).

II. Appointments That Do Not Comply With The Clause Undermine State Sovereignty.

Amici acknowledge that not every inferior federal officer can directly affect the States. For example, sovereigns almost certainly will not be respondents in an SEC enforcement action and thus subject to an SEC

ALJ's authority. Since SEC ALJs are the only persons whose status as officers is directly presented, *see* Pet'rs' Br. 42, this Court's judgment here will not immediately implicate *amici*'s workaday activities.

But *amici* care deeply about both *how* the Court answers that question and how the federal government *responds* to that answer. "[A]bout 150 ALJs in 25" other federal agencies also "apparently preside – as SEC ALJs do – over adversarial enforcement proceedings subject to Sections 556 and 557 of the" Administrative Procedure Act. *Id.* Because States can participate as sovereigns in some proceedings before other ALJs – and before other persons who similarly exercise significant federal authority – they have every incentive to ensure that those persons hold their offices lawfully.

Examples from Utah illustrate the point. The federal government administers 63.1 percent of the land within Utah's borders. Carol Hardy Vincent et al., Cong. Research Serv., R42346, *Federal Land Ownership: Overview and Data* 8 (2017), https://fas.org/sgp/crs/misc/R42346.pdf. Most of that land is managed by the Bureau of Land Management (within the Department of Interior) or the U.S. Forest Service (within the Department of Agriculture). *See id.* at 12.

The BLM and Forest Service processes for resolving challenges to their land-management decisions are charitably described as byzantine. Congress eventually had the Congressional Research Service summarize those processes because of their "complexity."

Kristina Alexander, Cong. Research Serv., R40131, *Administrative Appeals in the Bureau of Land Management and the Forest Service* i (2013), http://nationalaglawcenter.org/wp-content/uploads/assets/crs/R40131.pdf.

Consider just the BLM processes. The Department of Interior's Office of Hearing and Appeals (OHA) oversees administrative appeals. *See id.* at 1. "OHA is divided into two principal components: the appeals boards and the hearings division." *Id.* at 2. In public lands disputes, the Interior Board of Land Appeals "is the final step for most challenges of BLM agency actions (as distinguished from those based on land use plans)." *Id.* (citing 43 C.F.R. § 4.1(b)(3)). The decisionmakers on the Board are "Administrative Judges, which are distinct from Administrative Law Judges," though the BLM Director also "is an ex officio member." *Id.*

The hearings division, in contrast, "consists of ALJs, and is used where the law or regulations allow or require an ALJ." *Id.* That includes challenges to grazing decisions or certain types of oil and gas decisions. *See id.* What's more, "BLM officials" – with titles like "Deciding Officials" or "State Directors" – "also have authority to review disputes, typically at the early levels of a challenge." *Id.*

The upshot is that BLM resolves challenges to its land-management decisions through a host of procedures and decisionmakers. Administrative appeals of BLM land-use plans take one path when a State

governor files a "consistency review" (decision by the BLM State Director, appeal to the BLM Director, review in federal court) and another path when anyone else files a "protest" (decision by the BLM Director, review in federal court). *See id.* at 3-5. Any challenge to a BLM grazing decision begins with a "protest" resolved by a "deciding official," whose decision may be appealed to an ALJ, then to the Board, and then to federal court. *See id.* at 6-7. And parties challenge a BLM title or land-patent decision by filing a "contest" that an ALJ resolves; the losing party may appeal to the Board and then seek review in federal court. *See id.* at 9; 43 C.F.R. § 4.450.

Since the federal government controls nearly two-thirds of the land in Utah, the State is (and has been) a party in many BLM proceedings. *See, e.g.*, *Utah v. BLM*, No. 2017-200 (IBLA 2017); *S. Utah Wilderness All. v. BLM*, No. 2017-075 (IBLA 2017); *Wildearth Guardians v. BLM*, No. 2016-279 (IBLA 2016). Those proceedings directly implicate Utah's sovereign interests, and ineluctably raise questions like the one presented here: Are the BLM personnel who administer those proceedings inferior officers, and if so, did they take office consonantly with the Appointments Clause?

Amici do not ask this Court to answer those questions here. Nor do *amici* purport to answer them – for the BLM or for any federal agency whose personnel perform similar tasks. They merely note some pronounced similarities between SEC ALJs, *see* Pet'rs' Br.

20-26, and BLM decisionmakers.[2] The precise implications of those similarities must, of course, await the "case-by-case analysis" that *Freytag* requires. *Bandimere*, 844 F.3d at 1189 (Briscoe, J., concurring).

Yet just because the Court's opinion here will inform those later case-specific decisions about inferior officers – and may even create serious consequences for the federal government in the meantime – is no reason to shy away from Petitioners' requested outcome. The Court has not hesitated to resolve questions of similar magnitude despite its answers' potentially broad ramifications. Whether in prior Appointments Clause challenges, *see, e.g.*, *United States v. Germaine*, 99 U.S. 508, 511 (1878) (applying Appointments Clause to "thousands of clerks in the Departments of the Treasury, Interior and the othe[r]" departments), or in cases alleging other structural violations, *see, e.g.*, *New Process Steel, L.P. v. NLRB*, 560 U.S. 674, 676-78 (2010) (holding that the National Labor Relations Board had improperly delegated decision-making authority to a

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[2] *See, e.g.*, 43 C.F.R. § 4.1 (stating that BLM's OHA "is an authorized representative of the Secretary for the purpose of hearing, considering, and deciding matters within the jurisdiction of the Department involving hearings, appeals, and other review functions of the Secretary"); *id.* § 4.1(a) (BLM ALJs "are authorized to conduct hearings in cases arising under statutes and regulations of the Department"); *id.* § 4.1(b)(2) (the Board of Land Appeals "decides finally for the Department appeals to the head of the Department from decisions rendered by Departmental officials"); *id.* § 4.26(a) (BLM ALJs are "authorized to issue subpoenas," both "on [their] own motion, or on written application of a party"); *id.* § 4.438(c) (providing that an ALJ's decision "will be final for the Department unless a notice of appeal is filed").

two-person quorum, which had "decided almost 600 cases"), this Court decides cases as they come – irrespective of the consequences. So too here.

In fact, a pressing need exists for this Court's clear guidance precisely *because* the implications might sweep broadly. If the SEC has erred, other federal agencies might have, too. And if that means unconstitutional federal appointments abound – and directly affect sovereign States – neither the separation of powers nor federalism tolerates proverbially sweeping the debris under the rug. Better to announce clear rules so that the Executive and Legislative Branches can ensure that other rooms in our constitutional structure are properly cleaned.

* * * * *

Adherence to the Appointments Clause's strictures yields benefits for "the entire Republic," *Freytag*, 501 U.S. at 880 – including the States. *Amici* respectfully urge the Court to answer the question presented in a way that allows the entire Republic to assess whether persons exercising significant federal power do so lawfully.

CONCLUSION

The judgment of the Court of Appeals for the D.C. Circuit should be reversed.

Respectfully submitted.

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No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, ET AL., *Petitioners*,

v.

SECURITIES AND EXCHANGE COMMISSION, *Respondent*.

On Writ of Certiorari to the U.S. Court of Appeals for the District of Columbia Circuit

BRIEF FOR URSKA VELIKONJA AND JOSEPH A. GRUNDFEST AS *AMICI CURIAE* IN SUPPORT OF NEITHER PARTY

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INTEREST OF *AMICI*[1]

Amici curiae are law professors whose research and teaching focus, among other things, on empirical analysis of the enforcement of the federal securities laws. Joseph A. Grundfest is the William A. Franke Professor of Law and Business at Stanford Law School and served as Commissioner of the United States Securities and Exchange Commission ("SEC" or "Commission") from 1985 to 1990. Urska Velikonja is Professor of Law at Georgetown University Law Center.

We are, to the best of our knowledge, the only academics who have conducted empirical analyses of the outcomes of litigated matters filed by the SEC as administrative proceedings and in federal court. *See* Joseph A. Grundfest, *Fair or Foul? SEC Administrative Proceedings and Proposal for Reform Through Removal Legislation*, 85 FORDHAM L. REV. 1143 (2016); Urska Velikonja, *Are the SEC's Administrative Law Judges Biased? An Empirical Investigation*, 92 WASH. L. REV. 315 (2017); Urska Velikonja, *Reporting Agency Performance: Behind the SEC's Enforcement Statistics*, 101 CORNELL L. REV. 901 (2016); Urska Velikonja, *Securities Settlements in the Shadows*, 124 YALE L.J. F. 126 (2016), http://www.yalelawjournal.org/forum/securities-settlements-in-the-shadows. Professor Grundfest is also founder and principal investigator at the Stanford

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[1] All parties have consented in writing to the filing of all amicus briefs. No counsel for a party authored this brief in whole or in part, and no person other than *amici* or its counsel made a monetary contribution to the preparation or submission of this brief.

Securities Class Action Clearinghouse, an online resource that tracks activity in every federal class action securities fraud proceeding filed since the effective date of the Private Securities Litigation Reform Act of 1995, Pub L. 104-67, 109 Stat. 737. *See* securities.stanford.edu.

INTRODUCTION AND SUMMARY OF ARGUMENT

Briefs filed in this case cite to news articles alleging that the SEC is more likely to prevail in lawsuits decided by ALJs than in cases litigated in federal district courts.[2] These articles also contend that following the adoption of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. 111-203, 124 Stat. 1376, the Commission is more likely to litigate matters before administrative law judges than prior to the Act's adoption.

In particular, a Wall Street Journal article based on data analyzed by a Wall Street Journal reporter concludes that "'[t]he SEC brought more than four out of five of its enforcement actions' before its ALJs, 'up from less than half of them a decade earlier.'" Petition for Writ of *Certiorari* at 33, No. 17-130, 2017 WL 3189046 (filed July 21, 2017) (quoting Jean Eaglesham, *SEC Wins with In-House Judges*, WALL ST. J. (May 6, 2015) ("Eaglesham"). One *amicus*

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[2] *See, e.g., e.g.*, Petition for a Writ of *Certiorari* at 33, No. 17-130, 2017 WL 3189046 (filed July 21, 2017) (quoting Jean Eaglesham, *SEC Wins with In-House Judges*, WALL ST. J (May 6, 2015); Brief of the Chamber of Commerce of the United States of America as Amicus Curiae Supporting Petitioners at 9, No. 17-130, 2017 WL 3713062 (filed August 25, 2017) (citing Eaglesham).

asserts that "[b]etween October 2010 and March 2015, the SEC won 90% of the cases it brought before its ALJs, as compared with 69% of cases before district court judges." Brief of the Chamber of Commerce of the United States of America as *Amicus Curiae* Supporting Petitioners at 9, No. 17-130, 2017 WL 3713062 (filed August 25, 2017) (citing Eaglesham). Summarized differently, "[s]ince the Dodd-Frank Act of 2010 expanded the Commission's administrative enforcement authority, the Commission has brought more than 80% of its enforcement proceedings in its in-house tribunal, where it has won over 90% of the time." Brief for Petitioners at 3, No. 17-130, 2018 WL 1027816 (filed February 21, 2018) (citing Eaglesham). In much the same vein, an earlier New York Times article reported that, in its review of cases filed in 2011, the SEC prevailed in 88% of cases it filed before ALJs compared to 63% of cases it filed in federal district court. *See* Gretchen Morgenson, *At the SEC, a Question of Home-Court Edge*, N.Y. TIMES, Oct. 5, 2013, http://www.nytimes.com/2013/10/06/business/at-the-sec-a-question-of-home-court-edge.html.

Taken together, these articles foster the impression, relied upon by briefing in this case, that the Commission has a "home court" advantage when litigating before its administrative law judges. The articles also foster the impression that the Commission is filing more litigation as administrative proceedings to capitalize on this alleged advantage.

We take no position on the merits of this case and express no view as to its resolution. We also express no view as to the fairness or efficiency of the procedural rules governing the Commission's

administrative process.[3] Those questions are quite distinct from the constitutional question before the Court. Instead, we write exclusively to address two empirical questions raised by the debate over the Commission's reliance on administrative enforcement of the federal securities laws.

First, is there statistically reliable evidence that ALJs systematically resolve cases in a manner that differs from the resolution of equivalent Commission actions filed in federal district court?

Second, has the Commission steered a disproportionate share of contested proceedings to ALJs because the Commission is more likely to prevail before those ALJs?

Each of us has independently addressed these questions through empirical analyses that rely on different databases and that apply different analytic techniques. *See* Joseph A. Grundfest, *Fair or Foul? SEC Administrative Proceedings and Proposal for Reform Through Removal Legislation*, 85 FORDHAM L. REV. 1143 (2016); Urska Velikonja, *Are the SEC's Administrative Law Judges Biased? An Empirical Investigation*, 92 WASH. L. REV. 315 (2017). We have each independently reached identical conclusions. Contrary to the suggestions that appear in the press, there is no statistically reliable evidence that the Commission has a "home court" advantage before ALJs. There is also no statistically reliable evidence that the Commission is steering a disproportionate share of litigation to the administrative forum in order

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[3] For analysis of the fairness and efficiency of the procedures followed in the Commission's administrative proceedings, *see* generally Grundfest, *supra*, 85 FORDHAM L. REV. 1143 (2016).

to capitalize on this non-existent advantage. *See* Grundfest, *supra*, 85 FORDHAM L. REV. at 1175-84; Velikonja, *supra*, 92 WASH. L. REV. at 341-62.

To test whether these findings are robust to more recent enforcement decisions by the Commission, this *amicus* brief reports on the findings of an empirical analysis that examines every enforcement action filed by the SEC from the beginning of fiscal year 2007 through September 30, 2017, the end of the SEC's 2017 fiscal year, and resolved prior to January 1, 2018. We explain our data collection and classification methodology in the main body of our argument (at pp. 8-10) and document significant classification problems with the data upon which the Wall Street Journal and New York Times rely. Contrary to the conclusions reported in those articles and advanced in the briefing in this case, we find no statistically significant difference in the SEC's success rate in federal district court as opposed to before ALJs based on the analysis of the expanded dataset reported in this *amicus* brief. We also find that the SEC has continued to litigate a large majority of contested proceedings in federal district court, and not before its ALJs. Our analysis of the more recent data is thus also inconsistent with the suggestion of "home court" bias in matters litigated before the Commission's ALJs.

We are aware of no published academic study that reaches conclusions inconsistent with those expressed in this *amicus* brief, or with our prior articles addressing this question. We recognize, however, that the absence of a statistically significant difference in ALJ and federal district court resolutions as analyzed in this submission, and in our prior scholarship, cannot establish that there is no case, or set of cases,

in which outcomes before an administrative law judge and before a federal district court would not have differed. We are therefore not arguing that the forum in which a case is litigated is universally irrelevant.

Our analysis is, instead, based on comparisons of averages, and the data indicate that, on average, the forum is not outcome determinative. Moreover, the absence of a difference in average outcomes does not imply the absence of a difference in the perceived, *ex ante* probability of success by each litigant in each forum. In particular, we are unable to measure the quality of each case and the expected likelihood of success on the merits for either party in either forum. The implications of this limitation on the data are potentially significant. If, for example, the SEC is sending its stronger cases to ALJs, its success rates before ALJs should be higher than in federal court, all else being equal. Similarly, if the SEC is sending more difficult cases to ALJs, then the finding that there is no difference in average outcomes between the two forums would imply that the ALJ process is biased in favor of the SEC. If, however, the cases sent to the different forums have similar average chances of success on the merits, then our results imply that conclusions reported in the Wall Street Journal and relied on in the briefing have no empirical support and should not be relied on.

For these and other reasons described below, data describing win-loss ratios before ALJs and in federal court cannot, in and by themselves, establish the presence or absence of a "home court" advantage. We accordingly urge this Court to address all data of this sort, including the analyses presented in the Wall Street Journal, The New York Times, in our academic

publications, as well as in this *amicus* brief, with extreme caution. This Court should resolve the question presented through the application of standard interpretive techniques that do not refer to the empirical questions addressed in this *amicus* brief.

ARGUMENT

The Securities and Exchange Commission can often, but not always, exercise discretion as to whether to file an enforcement proceeding in an administrative forum or in federal district court. Some actions, such as proceedings seeking a temporary restraining order, an asset freeze, or the appointment of a receiver must be filed in federal court because only a federal court can order the remedy sought by the Commission. *See, e.g.*, Andrew Ceresney, Dir., SEC Div. of Enf't, Keynote Speech at New York City Bar 4th Annual White Collar Institute (May 12, 2015), https://www.sec.gov/news/speech/ceresney-nyc-bar-4th-white-collar-key-note.html. In contrast, the statutes require that the Commission file other actions as administrative proceedings, including actions to suspend or terminate the registration of public companies for failure to file periodic reports, follow-on proceedings to bar individuals or entities from the securities industry, or charges of failure to supervise employees who committed serious securities violations. *See e.g.*, 15 U.S.C. §§ 78l(j), 78o(b)(4). In most instances, however, the SEC can choose the forum in which it litigates contested cases.

Since 1990, the SEC has had the authority to seek monetary penalties, including civil fines, in administrative cease-and-desist proceedings, but only against registered persons, including broker-dealers

and investment advisers like the petitioners. *See* Securities Enforcement Remedies and Penny Stock Reform Act of 1990, §§ 102, 202-203, 301, 401, 104 Stat. 931, 933-35, 937-40, 941-44, 946-49. The Dodd-Frank Act expanded the Commission's powers to seek civil fines in administrative cease-and-desist proceedings to include actions against any individual or entity, regardless of whether they were registered with the Commission. Dodd-Frank thereby dramatically expanded the domain of cases in which the Commission could exercise discretion in forum selection while still obtaining substantial civil fines. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, § 929P, 124 Stat. 1376, 1862-64. Our analysis focuses on the subset of cases in which the Commission can exercise discretion over forum selection.

I. The SEC Brings a Small Minority of Contested Actions as Administrative Proceedings.

Media reports suggesting the existence of a "home court" advantage appear to rest on incomplete data collection and classification methodologies that are subject to material dispute.[4] To establish the foundation for this conclusion, we begin with a detailed explanation of our data collection methodology. To assemble the data set that informs our analysis, we rely principally on annual *Select SEC and Market Data* reports from 2007 to 2016, published by the Commission. *See e.g.*, SEC, Select SEC and

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[4] The media reports discussed in this *amicus* brief have not publicly disclosed the raw data upon which their conclusions are based, nor have they explained precisely how they collected, categorized, or analyzed their data.

Market Data Fiscal 2016, https://www.sec.gov/files/2017-03/secstats2016.pdf. These reports include a complete list of SEC enforcement actions filed in a given fiscal year. We supplement that list by reviewing administrative and court dockets to ensure that the data set is complete, and to add actions filed in fiscal 2017 for which the SEC has yet to release a report.

We exclude from the analysis all actions in which the SEC does not pursue an original violation of federal securities laws. We therefore exclude: (1) follow-on administrative proceedings in which the SEC seeks to suspend or bar a respondent previously found liable for violating securities and related laws; (2) Section 12(j)[5] actions to delist a company; (3) subpoena enforcement proceedings; and (4) contempt proceedings. The first two categories of listed actions can be filed *only* in an administrative proceeding; the latter two can be filed *only* in federal court. Thus, in no case that falls in any of these four categories does the Commission exercise any discretion as to forum selection. We find that in all of these actions, the Commission's success rate is substantially higher than in actions in which the Commission must establish liability for a predicate securities law violation. *See* Urska Velikonja, *Reporting Agency Performance: Behind the SEC's Enforcement Statistics*, 101 CORNELL L. REV. 901, 914-15 n.71 (2016). Unless otherwise indicated, we also exclude from our analysis resolutions predicated on collateral

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[5] 15 U.S.C. §§ 78l(j).

estoppel arising from a prior criminal conviction for the same violation.[6]

We tabulate and report the information both by defendant and by enforcement action. We present both forms of analysis separately to account for the fact that the SEC sues some defendants individually and joins others in a single action. There appears to be no systematic basis upon which the Commission decides whether to aggregate multiple defendants in a single action, or whether to file multiple individual actions against multiple defendants. As demonstrated below, our conclusions remain the same in every variation in categorization.

We also exclude from the analysis all relief defendants. These defendants are named in Commission complaints only so the agency can obtain disgorgement, and not so it can establish that any relief defendant violated any of the securities laws. We also review charging and related documents in each proceeding to determine whether the action was initially settled or contested, and whether the action was filed in federal court or as an administrative proceeding.

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[6] These actions ordinarily result from a joint investigation by civil and criminal authorities. Both civil and criminal authorities often file parallel charging documents on the same day. The SEC's case is then usually stayed until the criminal case is resolved. Once prosecutors have secured a guilty plea or conviction, the SEC moves for summary judgment or settlement. In our sample, the SEC wins all such summary judgment cases, and all but one of these cases were filed in federal court. Excluding these actions ensures that the data are not biased so as to inflate the Commission's success rate.

Our data indicate that, from fiscal 2007 through 2017, defendants' initial settlement rate in standalone actions varied from a low of 32% in fiscal 2009 to a high of 55% in fiscal 2015, with an average of 41%.[7] The number of settled actions initially filed as administrative proceedings increased considerably during this period. Between fiscal 2007 and 2010, before the Dodd-Frank amendments took effect, an average of 40% of settlements were filed as administrative proceedings.[8] That share increased to 83% in fiscal 2015. *See* Urska Velikonja, *Securities Settlements in the Shadows*, 124 YALE L.J. F. 126, 130 (2016) ("Velikonja, *Settlements*").

This increase in the percentage of settled actions filed as administrative proceedings is readily explained as a consequence of the bargaining dynamics in settlement proceedings that have no implication for the presence of an alleged SEC "home court" advantage before ALJs. In particular, Dodd-Frank allows both non-registered respondents and the Commission to settle matters as administrative proceedings whereas, prior to Dodd-Frank, precisely the same settlements would have been filed in federal court. If defendants perceive administrative cease-and-desist settlements to signal less culpability and to involve exposure less severe than that associated with the entry of a federal injunction, then defendants would, all other factors equal, prefer to settle a matter

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[7] These data include standalone actions filed in court and in administrative proceedings, and exclude follow-on and delinquent filing actions.

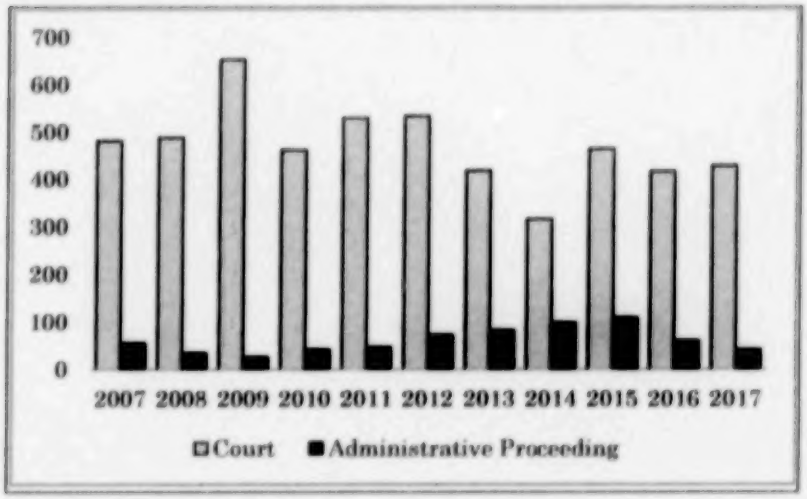
[8] This result is conditioned on a count of respondents, not of proceedings.

if it is filed as an administrative proceeding than if it is filed in federal court. The increase in settlements initially filed as administrative proceedings may therefore reflect defendant preferences more than strategic forum selection decisions on the part of the Commission. *See* Joseph A. Grundfest, *supra*, 85 FORDHAM L. REV. at 1151-52, 1182-83; Velikonja, *Settlements*, 124 YALE L.J. F. at 125-26.

But contrary to claims advanced in the Wall Street Journal and cited in the briefing, the *overall* share of *contested* cases (rather than *settled* cases) filed in administrative proceedings remains small post-Dodd-Frank, although the relative increase in the share of contested cases filed in administrative proceedings is substantial and statistically significant. *See* Urska Velikonja, *Are the SEC's Administrative Law Judges Biased? An Empirical Investigation*, 92 WASH. L. REV. 315, 342 (2017) ("Velikonja, *ALJ Bias*"). Between fiscal 2007 and 2010, 7% of respondents who did not initially settle with the SEC faced the agency in an administrative proceeding. By fiscal 2014, 23% of non-settling respondents faced the SEC in an administrative proceeding. The relative share of non-settling respondents sued in an administrative proceeding has since declined to pre-Dodd-Frank levels. *See* Figure 1.

FIGURE 1

Filings in Contested Cases by Forum (by Number of Defendants)[9]



* * *

In sum, the WSJ and related news stories incorrectly suggest that the SEC litigates a material percentage of contested actions before ALJs. At peak, 23% of non-settling respondents in standalone actions faced the SEC before an ALJ. Currently, about 7% of respondents do.

---

[9] Figure 2 in the Appendix shows filings in contested actions using the enforcement action as a unit of analysis. Between fiscal 2007 and 2010, 10% of enforcement actions that were not initially settled were filed as administrative proceedings. At peak in fiscal 2014, 38% of initially contested enforcement actions were filed as administrative proceedings.

II. The Data Reject the Hypothesis That the SEC Prevails More Frequently Before ALJs Than in Federal District Court.

Most defendants who initially contest the SEC's charges, whether in administrative proceedings or in federal court, ultimately settle. Our analysis of outcomes in contested actions excludes these settlements, and also excludes actions that result in a default judgment or voluntary dismissals. Our analysis therefore focuses exclusively on the outcomes of cases filed in fiscal years 2007 to 2017, in which a judge, a jury, or an ALJ issued a decision prior to January 1, 2018. These are the matters that are litigated fully to conclusion.

This sample includes federal court cases decided after a full jury or bench trial, cases decided by summary judgment, and cases dismissed on a contested motion to dismiss. The sample also includes administrative cases in which ALJs issued initial decisions that are not based on respondent's default, including cases in which the ALJ's decision has subsequently been appealed to the Commission[10] and the case remains pending. This sorting yields a list of 791 defendants in 374 enforcement actions, of whom 602 faced the SEC in court (in 273 enforcement actions) and 189 appeared before an ALJ (in 101 enforcement actions).

We measure outcomes as of the point of first decision on liability. That decision may be the result of

---

[10] In this Part II of the Argument, we use the term "the Commission" to refer to the five commissioners who review appeals to ALJ rulings. We use the term "SEC" to refer to the agency.

a partial summary judgment or a jury verdict that is later reversed on appeal. It could also reflect an ALJ initial decision that is later reversed by the Commission. The analysis considers only the outcome by the first court and the first ALJ to decide the matter as to defendant's or respondent's liability.[11]

A trial or summary judgment is deemed a victory for the SEC if it prevails on one or more claims against any defendant in a manner that entitles it to relief under the federal securities laws, even if no relief is ultimately awarded. A ruling or verdict for the SEC as to an element of an offense, absent a finding that a defendant actually violated a provision of the federal securities laws, is not counted as an SEC victory because the SEC would still have to establish that a violation occurred.

In Table 1 (pp. 16 and 17 below), we report our initial results by individual defendant and by enforcement action. In rows one, four, and five, we include cases predicated on a prior criminal conviction. In other rows, we exclude these cases. The first three rows report results using each defendant as a unit of analysis; rows four through nine report results by enforcement action. Notes included after Table 1 explain additional measurement variations we

---

[11] In some cases, the respondent or the SEC appeals the ALJ initial decision to the Commission, which then issues an opinion deciding the matter after *de novo* review. Of cases that were appealed to the Commission between fiscal 2008 and 2017, the Commission resolved the matter in favor of the respondent as often as it resolved it in favor of the SEC. As a result, our findings and conclusions would not be affected by including resolutions after appeal to the Commission. *See* Velikonja, *ALJ Bias*, 92 WASH. L. REV. at 325 n.63.

used as robustness checks. No matter how we slice the data, the SEC's relative success rate in either forum is consistently between 80 and 90 percent, and in no version of the analysis is there a statistically significant difference in success rates between the two forums.

TABLE 1

SEC Success Rate in Court and in Before an ALJ (2007-2017)

	Court	ALJ
By Defendant (1) (N_{Court} = 602; N_{ALJ} = 189)	88%	85%
By Defendant (2), (3) (N_{Court} = 508; N_{ALJ} = 188)	86%	85%
By Defendant (2), (4) (N_{Court} = 502; N_{ALJ} = 188)	87%	85%
By Enforcement Action (1), (3), (5) (N_{Court} = 273; N_{ALJ} = 101)	85%	83%
By Enforcement Action (1), (3), (6) (N_{Court} = 273; N_{ALJ} = 101)	87%	87%
By Enforcement Action (2), (5), (7) (N_{Court} = 212; N_{ALJ} = 100)	81%	83%
By Enforcement Action (2), (6), (7) (N_{Court} = 212; N_{ALJ} = 100)	83%	87%
By Enforcement Action (2), (5), (8) (N_{Court} = 222; N_{ALJ} = 100)	82%	83%
By Enforcement Action (2), (6), (8) (N_{Court} = 222; N_{ALJ} = 100)	84%	87%

(1) The tally includes summary judgments predicated on a prior guilty plea or conviction.

(2) The tally does not include summary judgments predicated on a prior guilty plea or conviction.

(3) Ten defendants faced parallel criminal proceedings. Where those proceedings were vacated on appeal, the SEC moved to vacate earlier entered settlements or obtained summary judgments. The tally includes them as SEC losses by summary judgment.

(4) Ten defendants faced parallel criminal proceedings and pleaded guilty or were convicted. On appeal, criminal judgments were reversed and the SEC moved to vacate settlements and summary judgments that it obtained on the basis of criminal judgments. These defendants are included in the tally as if the cases were not vacated.

(5) Counting as SEC wins only those multi-defendant actions where the SEC prevailed against all defendants.

(6) Counting as SEC wins those multi-defendant actions where the SEC prevailed against at least one defendant, but may have lost against some.

(7) Excluding from analysis multi-defendant cases, where at least one defendant's resolution is predicated on earlier guilty plea or conviction.

(8) Excluding from analysis multi-defendant cases, where all defendants' resolutions are predicated on earlier guilty pleas or convictions.

Because we study all actions filed in fiscal years 2007 through 2017, regardless of whether all cases filed in a given year have been resolved, concern arises that cases that remain ongoing are the cases that the SEC is more likely to lose. To address this concern, we

also report outcomes by year in which an action was originally filed (*see* Appendix, Figures 3.A and 3.C). All actions filed in fiscal years 2007 and 2008 have been resolved, and only a handful of actions filed in fiscal years 2009 to 2012 remain ongoing (five, one, two, and five cases, respectively). These counts exclude cases stayed for the duration of parallel criminal proceedings. We also report results by the year in which the action was resolved (*see* Appendix, Figures 3.B and 3.D). A year-to-year comparison in outcomes is considerably more variable, as is common when the sample size is small, but there are no obvious trends suggesting that the SEC is more likely to lose actions that take longer to resolve. The presence of ongoing cases is therefore unlikely to change our overall result reported above: the SEC prevails against defendants at very high rates in administrative proceedings and in federal district court, and there is no statistically significant difference in the SEC's success rate between the two forums.

Insider trading cases are, however, different. As shown in Figure 4 in the Appendix, the SEC loses about half of insider trading cases decided both by courts and by ALJs, whereas its success rate in other types of actions is much higher. Insider trading cases represent 9% of contested cases studied but 33% of SEC losses overall. Of contested cases filed in federal district court, insider trading cases represent 12% of our sample but 42% of SEC losses. Of contested cases litigated before ALJs, insider trading cases represent only 2% of the sample, but 7% of all losses. The SEC's success rate before federal district courts and before ALJs in insider trading cases is statistically

indistinguishable. However, because insider trading cases represent a much larger share of the SEC's losses in federal district court, and a much smaller share of its losses before ALJs, any comparison of success rates in these two forums that fails to account for this important variation in case characteristics will be biased.

To address variation in case and defendant characteristics, we apply multivariate logistic regression techniques to test whether there is a statistically significant correlation between the likelihood that the SEC will prevail in an action and the forum in which the matter is litigated. We categorize defendants and actions by subject matter as reported in *Select SEC and Market Data* reports (*i.e.*, broker-dealer, insider trading, investment advisor, issuer reporting, market manipulation, and securities offering cases).[12] We also control for whether the defendant is an individual or an entity and, in some specifications, whether the resolution is based on prior criminal pleas or convictions.

We first analyze the entire dataset using a range of specifications, as described in the discussion of

---

[12] Four FCPA cases in our sample were treated as issuer reporting cases, consistent with the SEC's categorization of these actions before fiscal 2011. Eight municipal offering cases were treated as securities offering cases, and six cases against registered transfer agents were treated as investment adviser actions, again consistent with the SEC's categorization of these cases before fiscal 2011. Success rates in FCPA, municipal offering, and registered transfer agent cases are comparable to the SEC's success rate in the categories into which those cases were merged by the Commission (*i.e.*, the SEC prevailed in 3 of 4 FCPA actions, which is consistent with its success rate in issuer reporting cases generally).

Table 1. We then focus on cases filed in fiscal years 2007 to 2012, where all or nearly all cases have been resolved. We then analyze resolutions handed down in the years spanning 2012 to 2017, during which our dataset includes all or nearly all actions that have been resolved in a given fiscal year. We perform the analysis with the observations defined by individual defendant as well as by enforcement action. Select regression results are reproduced in the Appendix, Tables 2.A, 2.B, and 2.C. Our data set and the full set of regression results are available on-line at https://scholarship.law.georgetown.edu/scb/79/.

The forum in which a proceeding was heard, whether federal district court or administrative, was not significantly correlated with outcomes in all but 3 of 33 regression analyses (using the standard 5% level of significance).[13] In those three analyses, the results suggest that the SEC is at a *dis*advantage when litigating before ALJs. In no specification do we find evidence of home court *advantage*. The results are robust. As explained in Table 1, the data are coded several different ways to account for the presence of multi-defendant actions and for parallel guilty pleas, and we perform analyses of every variation.

* * *

Our conclusions differ from those reported in the Wall Street Journal and New York Times for several reasons. First, we include in our analysis all resolutions handed down by a third-party adjudicator, such as summary judgments, and do not rely

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[13] One of three statistically significant outcomes, suggesting that the SEC is at a disadvantage when litigating before ALJs, is reported in Table 2.C in the Appendix.

exclusively on cases decided after a trial or hearing. Inasmuch as a victory at the summary judgment stage is every bit as valuable as a victory after trial—indeed, it can be argued that a victory at summary judgment is a superior measure of the merits of a litigant's position—there appears to be no coherent reason to exclude summary judgments from the analysis. Thus, to the extent that the SEC tends to prevail more frequently at the summary judgment stage, as appears to be the case,[14] the exclusion of summary judgment and other pre-trial resolutions biases the data against the SEC.

Second, our analysis adjusts for the fact that forum selection is not random across all types of cases. The SEC tends to litigate certain types of cases more frequently in federal district court (*e.g.*, insider trading and offering fraud cases) and other types of cases more frequently before ALJs (*e.g.*, broker-dealer and investment advisor violations). This distinction is significant from an analytical perspective because the SEC is more likely to lose when litigating insider trading claims than is it to lose when litigating other types of securities law violations, regardless of forum. Unless an analysis properly controls for this factor, it is easy to reach the mistaken conclusion that the SEC's success rate in federal district court is lower than it is before ALJs, when, in reality, the finding

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[14] In our sample, the SEC prevailed at summary judgment against 408 of 423 defendants (a 96.4% win rate). Even if summary judgments based on prior convictions or guilty pleas are excluded, the SEC prevailed at summary judgment against 310 of 325 defendants (a 95.4% win rate). The SEC's win rate at summary judgment is higher than in cases decided after trial. *See also* Velikonja, *ALJ Bias*, 92 WASH. L. REV. at 349.

should be that the SEC's success in litigating insider trading actions is lower than its success in litigating other types of claims, and that insider trading cases are litigated overwhelmingly in federal district court, not in administrative proceedings.

III. Empirical Analysis of the Outcome of Contested Enforcement Proceedings Sheds No Light on the Question Presented in this Case.

The absence of a statistically significant difference in the resolution of matters litigated in federal district court and in administrative proceedings does not mean that there is no case, or no set of cases, in which outcomes in those individual cases would not have differed if litigated in a different forum. Thus, we do not claim that the choice of forum is irrelevant in every instance. Instead, the proposition advanced in our analysis is, instead, that the forum selection decision seems not to have an effect when measured on average.

Three additional caveats bear mention in connection with any analysis of outcomes in litigated enforcement proceedings. First, these analyses consider only outcomes in litigated matters, but most SEC enforcement actions are settled, including the majority of actions that are initially contested. A relatively higher share of defendants sued in court settle than do respondents who litigate before ALJs. As noted above, we cannot measure the quality of each type of case. But if the cases are similar in both forums, then defendants' greater willingness to settle in cases filed in federal district court biases the

comparison in favor of a higher SEC success rate in administrative proceedings.[15]

Second, the SEC does not litigate every case to conclusion. Instead, the Commission will move to dismiss the action where further prosecution of an entity is deemed unnecessary because the sole owner has been convicted or has died, because a parallel settled action is filed in an administrative proceeding, or for a variety of other reasons that often are not specified. Courts regularly grant these motions. Because researchers are unable to define precisely the cases that are voluntarily dismissed for these procedural reasons, rather than for other more substantive causes related to the merits, we exclude these observations from our analysis. The existence of these voluntary dismissals for indeterminate reasons generates noise in the data that complicates the ability to make strong assertions regarding the effects of SEC forum selection decisions.

Third, and most important, a finding that there is no average difference in outcomes between matters litigated in federal district court and matters litigated in administrative proceedings does not imply that there is no difference in the *a priori* probability of success in each forum. Contested actions filed in court and in administrative proceeding are similar on average, but not identical. Courts are more likely to

---

[15] For example, if defendants with a 30% or lower chance of success are more likely to settle when the action is litigated in court than before an ALJ, the pool of contesting litigants in federal district court will include fewer defendants with a low chance of success and more who face better odds. As a result, all else equal, the SEC's expected success rate in court should be lower than before an ALJ.

find that the defendant violated scienter-based provisions of securities laws than are ALJs, but court cases are somewhat less likely to result in a defendant's bar or suspension from the securities industry or from practicing before the Commission as accountant or attorney. *See* Velikonja, *ALJ Bias*, 92 WASH. L. REV. at 356-57. Median civil fines imposed in both forums are similar, but at the 75th percentile, the civil fines are higher in federal district court. *Id.* at 356. Thus, if the SEC systematically directs easier-to-win cases to ALJs, its success rates before ALJs should be higher, all other factors equal. Similarly, if the SEC systematically directs its more difficult cases to ALJs, then the absence of a statistically significant difference in outcomes would imply that the ALJs process is biased in favor of the SEC. If, however, the cases sent to each forum have similar chances of success on the merits on average, then our results imply that widely-reported press analyses suggesting a "home court" advantage in administrative proceedings would be incorrect.

* * *

We urge the Court to ignore references to statistical disparities in outcomes, suggestions that the SEC has a "home court" advantage in administrative proceedings, and that ALJs have a bias observable through the analysis of aggregate data. Every published academic study of which we are aware, and the additional analysis reported in this *amicus* brief, supports the conclusion that there is no statistically significant difference in the SEC's probability of prevailing in federal district court or in an administrative proceeding. We further emphasize that our conclusions should not be over-interpreted to

imply an absence of ALJ bias in any one case, or in any set of cases. Moreover, because researchers cannot evaluate *ex ante* case quality, or account for other selection biases, a comparison of outcomes in contested enforcement actions can only support cautious, qualified conclusions about the potential presence or absence of bias in any forum.

CONCLUSION

Amici end where we began. We take no position on the merits of this case and express no views as to its resolution. We also take no position as to the fairness or efficiency of the procedural rules governing the ALJ process, which is a question distinct from the one before the Court. Instead, we urge the Court to address the question presented as a matter of constitutional interpretation as to which the available statistical evidence provides no meaningful insight.

Respectfully submitted,

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February 28, 2018

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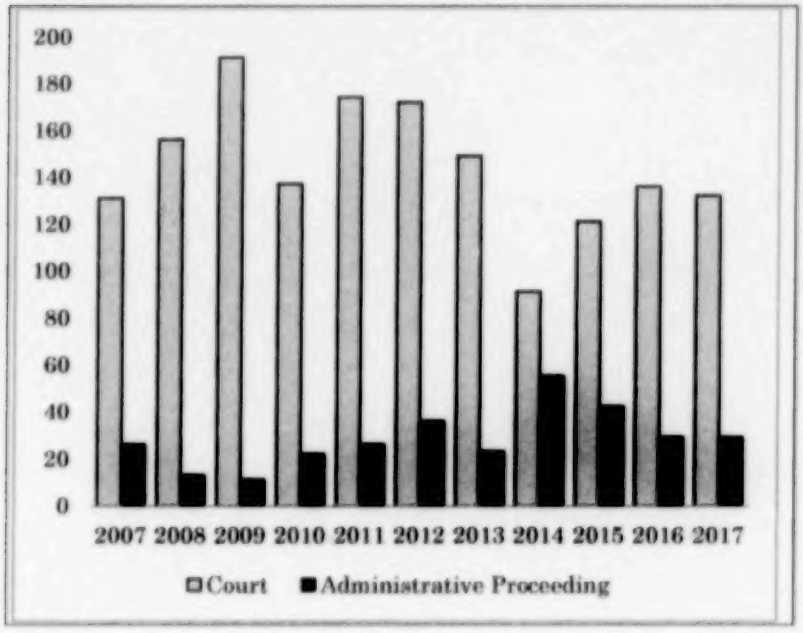
APPENDIX: DATA AND TABLES

FIGURE 2

Contested Actions Filings (enforcement action as the unit of analysis)



App. 2

FIGURE 3.A

Success Rate by Year of Filing (by defendants)

Success rate is tallied by individual defendant and by the fiscal year in which the action is filed. The tally does not include summary judgments based on prior conviction or guilty plea. $N_{Court} = 508$, $N_{ALJ} = 188$

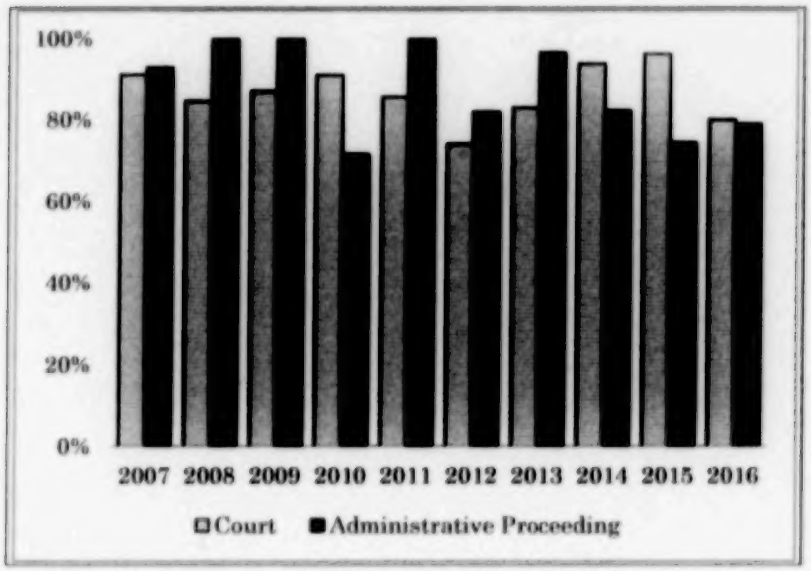


FIGURE 3.B

Success Rate by Year of Resolution (by the number of defendants)

Success rate is tallied by individual defendant and by the fiscal year in which the action is resolved. The tally does not include summary judgments based on prior conviction or guilty plea, but does include ten defendants whose settlement or summary judgment loss against the SEC was vacated. N_{Court}=508, N_{ALJ}=188.

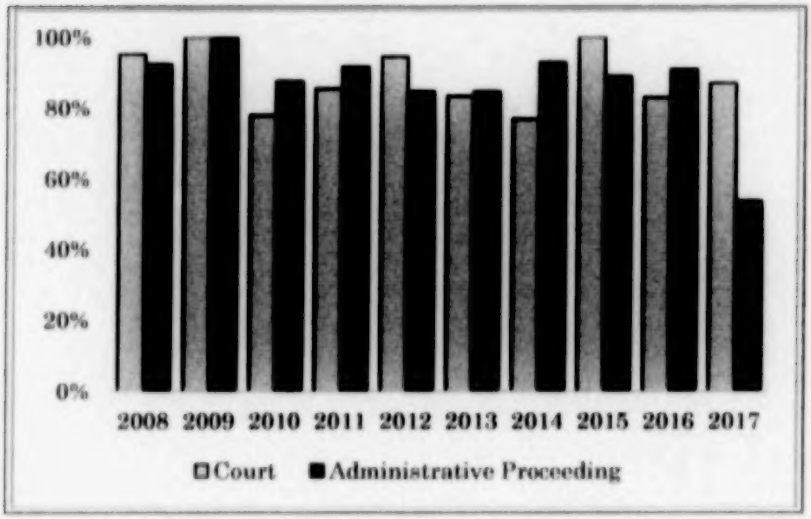


FIGURE 3.C

Success Rate by Year of Filing (enforcement action as the unit of analysis)

Success rate is tallied by enforcement action and by the fiscal year of filing. The tally does not include summary judgments based on prior conviction or guilty plea but does include ten defendants whose settlement or summary judgment loss against the SEC was vacated. $N_{Court} = 212$, $N_{ALJ} = 100$.

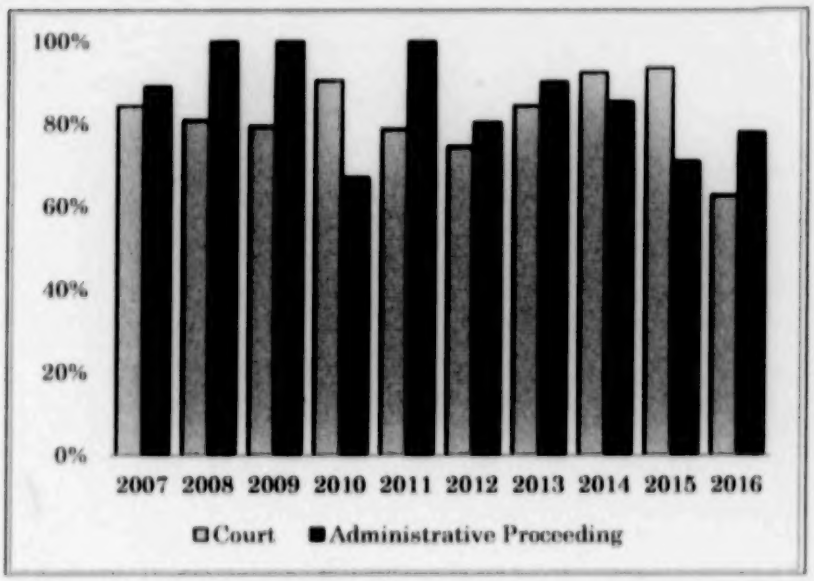


FIGURE 3.D

Success Rate by Year of Resolution (enforcement action as the unit of analysis)

Success rate is tallied by enforcement action and by the fiscal year in which the action is resolved. The tally does not include summary judgments based on prior conviction or guilty plea, but does include defendants whose settlement or summary judgment loss against the SEC was vacated. $N_{Court} = 212$, $N_{ALJ} = 100$.

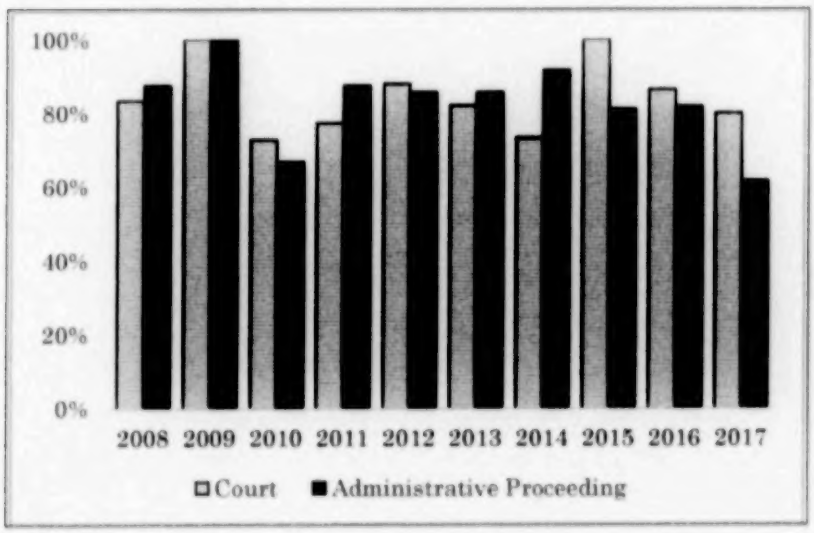
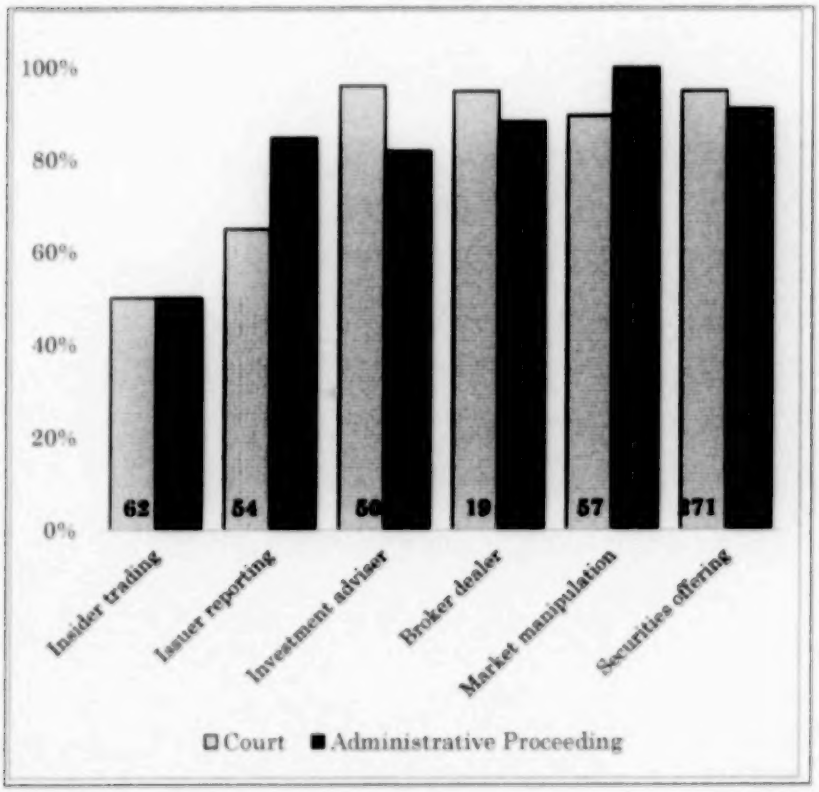


FIGURE 4

SEC's Success Rate by Type of Case (by defendant)

The figure does not include summary judgments predicated on collateral estoppel. The number of defendants in each case category is bolded.



Logistic Regression Results

The following list describes the various permutations we used when analyzing the data. We analyzed every permutation for the entire dataset. We separately analyzed cases filed between 2007 and 2012, where all or nearly all cases have been resolved, and resolutions handed down in the years spanning 2012 to 2017, during which our dataset includes all or nearly all actions that have been resolved in a given fiscal year. We performed the analysis with the observations defined by individual defendant as well as by enforcement action.

We reproduce some regression results in Tables 2.A, 2.B, and 2.C below. We report statistical significance using conventional methods (*** $p<0.01$; ** $p<0.05$). Standard errors are reported in parentheses.

The list of permutations used in regression analyses:

(1) The tally includes summary judgments predicated on a prior guilty plea or conviction.

(2) The tally does not include summary judgments predicated on a prior guilty plea or conviction.

(3) Ten defendants faced parallel criminal proceedings. Where those proceedings were vacated on appeal, the SEC moved to vacate earlier entered settlements or obtained summary judgments. The tally includes them as SEC losses by summary judgment.

(4) Ten defendants faced parallel criminal proceedings and pleaded guilty or were convicted. On appeal, criminal judgments were reversed and the SEC moved to vacate

settlements and summary judgments that it obtained on the basis of criminal judgments. Such defendants are included in the tally as if the cases were not vacated.

(5) Counting as SEC wins only those multi-defendant actions where the SEC prevailed against all defendants.

(6) Counting as SEC wins those multi-defendant actions where the SEC prevailed against at least one defendant, but may have lost against some.

(7) Excluding from analysis multi-defendant cases, where at least one defendant's resolution is predicated on earlier guilty plea or conviction.

(8) Excluding from analysis multi-defendant cases, where all defendants' resolutions are predicated on earlier guilty pleas or convictions.

TABLE 2.A

Logistic Regression Results (2007-2017)

	By Defendant					
	(1)	(1)	(2), (3)	(2), (3)	(2), (4)	(2), (4)
Forum ALJ	-.235 (0.24)	-.195 (0.32)	-.044 (0.24)	-.195 (0.32)	-.176 (0.25)	-.244 (0.31)
Entity Def.		.827*** (0.31)		.827*** (0.31)		.747** (0.31)
Case Category		***		***		***
	N=793	N=695	N=697	N=695	N=688	N=686

*** $p<0.01$; ** $p<0.05$. Standard errors are reported in parentheses.

TABLE 2.B

Logistic Regression Results (for cases filed between fiscal 2007 to 2012)

	By Defendant		By Enforcement Action	
	(2), (3)	(2), (3)	(2), (5), (7)	(2), (5), (7)
Forum ALJ	.300 (0.38)	-.098 (0.53)	.467 (0.48)	.282 (0.61)
Entity Defendant		1.823*** (0.31)		
Case Category		***		***
	N=472	N=471	N=203	N=202

*** p<0.01; ** p<0.05. Standard errors are reported in parentheses.

TABLE 2.C

Logistic Regression Results (for cases resolved between fiscal 2012 and 2017)

	By Defendant		By Enforcement Action	
	(2), (3)	(2), (3)	(2), (5), (7)	(2), (5), (7)
Forum ALJ	-.232 (0.27)	-.723** (0.37)	-.070 (0.37)	-.475 (0.48)
Entity Defendant		.33 (0.33)		
Case Category		***		***
	N=494	N=493	N=219	N=218

*** p<0.01; ** p<0.05. Standard errors are reported in parentheses.

No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA
AND RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF WASHINGTON LEGAL FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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February 28, 2018

QUESTION PRESENTED

Whether administrative law judges of the Securities and Exchange Commission are "Officers of the United States" under the Appointments Clause.

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INTEREST OF *AMICUS CURIAE*[1]

Washington Legal Foundation (WLF) is a nonprofit, public-interest law firm and policy center with supporters in all 50 states. WLF devotes a good deal of its resources to promoting free enterprise, individual rights, limited government, and the rule of law. To that end, WLF often engages in original and *amicus* litigation to prevent the accumulation of power in any one governmental branch in violation of the Constitution's careful separation of powers. *See, e.g., Gordon v. CFPB*, *cert. denied*, 137 S. Ct. 2291 (2017); *NLRB v. SW Gen., Inc.*, 137 S. Ct. 929 (2017); *Free Enter. Fund v. PCAOB*, 561 U.S. 477 (2010).

WLF has long criticized the Securities and Exchange Commission's (SEC) growing tendency to enforce federal securities laws before its own administrative law judges (ALJs) rather than Article III judges. Recent experience shows that the SEC nearly always prevails in its own in-house proceedings but is far less successful when it litigates in federal court. Given the significant federal authority the SEC's ALJs exercise in adjudicating complex and novel securities cases, WLF believes it is imperative that their appointment comport with the Appointments Clause of Article II, Section 2, which provides a vital check on runaway

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[1] Under Supreme Court Rule 37.6, WLF states that no counsel for any party authored this brief in whole or in part; and that no person or entity, other than WLF and its counsel, made a monetary contribution intended to fund the preparation and submission of this brief. All parties have filed blanket consents to the filing of *amicus curiae* briefs.

agency overreach in our constitutional system.

WLF takes no position on whether petitioners' conduct violated federal securities laws. Instead, it is filing this brief solely for the purpose of addressing the important constitutional issues raised by the question presented. Given the Appointment Clause defect at issue, WLF is concerned that if such Article II violations have no consequence because Executive Branch agencies may simply "ratify" *ultra vires* acts by improperly appointed agents, there will be little incentive to comply with the Appointments Clause in the future.

STATEMENT OF THE CASE

The relevant facts are set out in more detail in petitioners' brief. WLF wishes to highlight several facts of particular relevance to the issues on which this brief focuses.

The Administrative Procedure Act (APA) authorizes executive agencies such as the SEC to conduct administrative proceedings before an ALJ. Under 5 U.S.C. § 3105, "[e]ach agency shall appoint as many [ALJs] as are necessary for proceedings" where the applicable statute requires an adjudication on the record after an opportunity for a hearing. *See* 5 U.S.C. §§ 553, 556, & 557.

The SEC's relevant Rule of Practice, 17 C.F.R. § 201.110, provides that the SEC "shall" preside over all administrative proceedings either by the Commissioners' handling the matter themselves or by delegating the case to an ALJ. When the SEC selects an ALJ to preside over an administrative

proceeding—as the SEC did here—the Chief Administrative Law Judge makes that selection, subject to approval by the SEC's Office of Human Resources. Pet. App. 295a-297a; 17 C.F.R. § 201.110.

In its capacity as a hearing officer in an SEC enforcement proceeding, an ALJ "shall have the authority to do all things necessary and appropriate to discharge his or her duties." 17 C.F.R. § 201.111. Among those powers, the ALJ may administer oaths and affirmations; issue, revoke, quash, or modify subpoenas; receive and rule on the admission of relevant evidence; regulate the course of a proceeding and the conduct of the parties and counsel; and rule upon "all procedural and other motions." *See* 17 C.F.R.§ 201.111(a)-(d), & (h).

Once selected, the ALJ then presides over the matter, which includes an evidentiary hearing, and issues a decision. 17 C.F.R. § 201.360(a)(1). If no appeal follows and the SEC declines to review the ALJ's decision, that decision is "deemed the action of the Commission," 15 U.S.C. § 78d-1(c), and the SEC issues an order finalizing the ALJ's decision, 17 C.F.R. § 201.360(d)(2). Any party aggrieved by a final order of the SEC may petition a federal court of appeals for judicial review of that order.

Petitioners are formerly registered investment advisers who marketed a wealth-management strategy for retirement investors. Pet. App. 38a-41a. The SEC began administrative proceedings against petitioners and charged them with violating the Securities Exchange Act, the Investment Advisers Act, and the Investment Company Act. *Id.* at 238a. The SEC assigned the proceeding to ALJ Cameron

Elliot, who—during a nine-day hearing—presided over witness testimony, admitted documentary evidence, and ruled on objections. *Id.* at 116a. Following the hearing, the ALJ first determined that petitioners had fraudulently misrepresented one of their investment strategies. *Id.* at 117a.

After making supplemental factual findings about other alleged misrepresentations, the ALJ revised its decision to include a finding that petitioners willfully misled investors in violation of the Investment Adviser's Act. Pet. App. 195a-225a. The ALJ also imposed many sanctions on petitioners, including a revocation of their registrations as investment advisers, an injunction against future violations of the law, and $300,000 in civil penalties. *Id.* at 225a-235a.

The SEC confirmed the ALJ's factual findings and mostly affirmed—"with limited exceptions"—the ALJ's imposed sanctions. *Id.* at 66a-107a. Petitioners argued on appeal that the administrative proceedings against them were constitutionally infirm because the SEC's ALJ was an "Officer of the United States" who was never appointed under the Appointments Clause "by the President, the head of a department, or a court of law." Pet. App. 86a-87a. In rejecting that argument, the SEC held that its ALJs were employees, not executive officers, because they do not exercise "significant authority independent of the SEC's supervision." Pet. App. 88a.

Petitioners appealed the SEC's order to the court of appeals, which denied the petition for review. Pet. App. 3a-36a. Rejecting petitioners'

Appointments Clause challenge, the appeals court agreed with the SEC that its ALJs are employees who "do not exercise significant authority pursuant to the laws of the United States." *Id.* at 11a. Relying on its prior decision in *Landry v. FDIC*, 204 F.3d 1125, 113-34 (D.C. Cir. 2000), *cert. denied*, 531 U.S. 924 (2000), which upheld the validity of the Federal Deposit Insurance Corporation's (FDIC) ALJs against a similar challenge, the appeals court held that decisions of the SEC's ALJs are similarly non-final and thus not authoritative enough to constitute an action of the SEC. *Id.* at 12a-19a.

The appeals court also distinguished the SEC's ALJs from the Special Trial Judges of the Tax Court, whom this Court found to be executive officers in *Freytag v. Commissioner*, 501 U.S. 868 (1991). The appeals court reasoned that, unlike the SEC's ALJs, "the Tax Court in *Freytag* was required to defer to the special trial judge's factual and credibility findings unless they were clearly erroneous." Pet. App. 19a. Because the Special Trial Judges could "issue final decisions in at least some cases" they could "exercise the judicial power of the United States." *Id.* at 11a, 12a.

Concluding that ample evidence supported the SEC's finding that petitioners violated the Investment Adviser's Act, Pet. App. 21a-32a, the appeals court went on to hold that the SEC had not abused its discretion in imposing sanctions and monetary penalties on petitioners. *Id.* at 33a-36a.

Petitioners sought rehearing en banc. Pet. App. 244a-246a. The appeals court first granted rehearing, directed additional briefing, and vacated

the panel's judgment. In June 2017, however, the en banc court issued a per curiam ruling denying the petition for review "by an equally divided court." *Id.* at 1a-2a.

After the Solicitor General confessed error by conceding in its certiorari-stage brief that all SEC ALJs are "Officers" under the Appointments Clause, the SEC entered an order claiming to "put to rest" any constitutional defect. *See* Order, *In re Pending Administrative Proceedings*, Securities Act Release No. 10,440, at 1 (Nov. 30, 2017) (Ratification Order). The SEC purported to "ratify" the prior appointment of its five ALJs and directed them to "[r]econsider the record" in any open proceeding to decide "whether to ratify or revise in any respect all prior actions taken." *Id.* at 1-2.

SUMMARY OF ARGUMENT

By prescribing the exclusive means for appointing any "Officer of the United States," the Appointments Clause safeguards the Constitution's "structural integrity" by ensuring that those who wield significant federal authority are "accountable to political force and the will of the people." *Freytag*, 501 U.S. at 878, 884. But political accountability is a dead letter if, as here, agency decision-makers do not have to answer for their policy decisions to one of the elected branches.

The ALJ who presided over petitioners' hearings in this case was an "inferior Officer" within the meaning of Article 2, Section 2, Clause 2 of the Constitution. That provision requires that all "inferior Officers" be appointed by the President, the

"Courts of Law," or the "Heads of Departments." Petitioners' ALJ was not so appointed. That violation of the Appointments Clause renders unconstitutional the proceedings below and the resulting order against petitioners.

As this Court recognized in *Freytag*, Appointments Clause violations go "to the validity" of the underlying proceedings. 501 U.S. at 879. As its ratification order makes clear, however, the SEC deems any structural constitutional defect in its ALJ proceedings to be of no consequence. But this Court's precedents bar any effort to salvage *ultra vires* administrative hearings conducted by officials in violation of the Appointments Clause. Indeed, regardless of the name that government officials have previously used when trying to salvage proceedings conducted by improperly appointed officials—whether the *de facto* officer doctrine, harmless error analysis, or ratification—the Court has consistently rejected such efforts when (as here) the defendant has raised a timely objection to the qualifications of the presiding officer.

WLF urges the Court to address the propriety of the SEC's attempted "ratification" now, rather than allow the issue to drag on for several more years—particularly because this precise issue is almost certain to return to the Court. As detailed below, the Court should rule that any enforcement proceedings conducted before an improperly appointed ALJ are a nullity, and so the SEC must start from scratch if it chooses to renew enforcement efforts against the targets of those proceedings. Otherwise, if such clear constitutional violations can be so easily "ratified," little will be left of the

Constitution's "structural integrity" and the political accountability it guarantees.

ARGUMENT

I. BECAUSE THE SEC'S ALJS ARE OFFICERS OF THE UNITED STATES, THEIR APPOINTMENT BY THE CHIEF ALJ VIOLATES THE APPOINTMENTS CLAUSE

The Constitution divides federal power among three co-equal branches: Legislative, Executive, and Judicial. The Framers implemented this tripartite separation of powers to "provide avenues for the operation of checks on the exercise of governmental power." *Bowsher v. Synar*, 478 U.S. 714, 722 (1986). To help accomplish that important aim, the Constitution vests the Executive power in the President, who must "take Care that the Laws be faithfully executed." U.S. Const. Art. II, § 3.

Of course, the "President alone and unaided could not execute the laws. He must execute them by the assistance of subordinates." *Buckley v. Valeo*, 424 U.S. 1, 135 (1976) (quoting *Myers v. United States*, 272 U.S. 52, 117 (1926)). Article II of the U.S. Constitution carefully circumscribes the category of individuals authorized to exercise Executive Branch power. In particular, the Appointments Clause prescribes how such "Officers" of the United States must be chosen and appointed:

> [The President] shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls,

> Judges of the Supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

U.S. Const. Art. II, § 2, Cl. 2. As shown below, because the SEC's ALJs are "inferior Officers" under the Appointments Clause, their appointment by the Chief ALJ is unconstitutional. Because that defect "goes to the validity of the ... proceeding," *Freytag*, 501 U.S. at 879, this Court should vacate the SEC's final opinion and order below.

A. The SEC's ALJs Are Inferior Officers of the United States

By its own terms, the Appointments Clause provides that "Congress may by law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments." U.S. Const. Art. II, § 2, Cl. 2; *Buckley*, 424 U.S. at 132. Here it is undisputed that the appointment of the ALJ who presided in petitioners' case did not satisfy that constitutional command. Instead, petitioners' ALJ was selected by the SEC's Chief ALJ, subject to approval by the SEC's Office of Human Resources. Pet. App. 295a-297a; 17 C.F.R. § 201.110.

Where, as here, an individual "exercise[s] significant authority pursuant to the laws of the United States," that person "is an Officer of the United States." *Freytag*, 501 U.S. at 881. In *Freytag v. Commissioner*, this Court concluded that the Special Trial Judges (STJs) appointed by the Chief Judge of the Tax Court were inferior officers whose appointment violated the Appointments Clause. In so holding, the Court focused on (1) the fact that the office of the STJ was "established by Law ... and the duties, salary, and means of appointment for that office [were] specified by statute," and (2) that the STJs performed "more than ministerial tasks." 501 U.S. at 881-82. The SEC's ALJs resemble STJs in all those respects.

As was true of the STJs in *Freytag*, the office of an SEC ALJ is established by law. An SEC ALJs' duties, salary, and means of appointment are all determined by statute. *See, e.g.*, 5 U.S.C. § 556 (establishing powers and duties of ALJs presiding over administrative hearings); 5 U.S.C. § 557(b) (providing that an ALJ must "initially decide the case"); 5 U.S.C. § 3105 ("Each agency shall appoint as many [ALJs] as are necessary for the proceedings required to be conducted in accordance with sections 556 and 557 of this title."); 5 U.S.C. § 5372 (establishing the salary of ALJs). And the Securities Exchange Act of 1934 itself confirms the ALJ's broad authority. *See* 15 U.S.C. § 78d-1(a) (providing that the SEC "shall have the authority to delegate ... any of its functions to ... an administrative law judge ... including functions with respect to hearing ... any ... matter").

Entrusted with broad powers, the SEC's ALJs perform more than "ministerial tasks." Like the STJs in *Freytag*, the SEC's ALJs regularly take testimony, conduct trials, make evidentiary rulings, and impose sanctions. *See, e.g.*, 17 C.F.R. § 200.14 (establishing an ALJ's broad powers in proceedings instituted by the SEC); 17 C.F.R. § 200.30-9 (describing the delegation of significant authority from the SEC to each ALJ "hearing officer"); 17 C.F.R. § 200.30-10 (describing the delegation of authority from the SEC to the Chief ALJ); 17 C.F.R. § 200.111 (establishing the authority of a "hearing officer"); 17 C.F.R. § 201.180 (authorizing the ALJ to impose sanctions for contemptuous conduct). To be sure, the fact that the SEC authorizes its ALJs to "[r]egulate the course of a hearing," 17 C.F.R. § 200.14, confirms that they exercise "significant discretion" in "carrying out the[ir] important functions." *Freytag*, 501 U.S. at 882.

The SEC's ALJs resemble *Freytag*'s STJs in another important respect: both may render final decisions. As an alternative holding, *Freytag* noted that STJs were inferior officers because they could render decisions of the Tax Court in some classes of cases, subject to whatever review the Tax Court may care to provide. 501 U.S. at 882. ALJs may also render final decisions of the SEC in some cases. *See* 5 U.S.C. § 557(b) (explaining that when an ALJ "makes an initial decision, that decision then becomes the decision of the agency without further proceedings unless there is an appeal to, or review on motion of, the agency within the time provided by the rule"). Ultimately, if the SEC opts not to review a decision of the ALJ, "then the action of [the ALJ]

... shall, for all purposes, including appeal or review thereof, be deemed an action of the Commission." 15 U.S.C. § 78d-1(c).

Although *Freytag* did not address whether ALJs constitute inferior officers of the United States, Justice Scalia answered that question in his concurring opinion:

> Today, the Federal Government has a corps of administrative law judges numbering more than 1,000, whose principal statutory function is the conduct of adjudication under the Administrative Procedure Act ("APA"), *see* 5 U.S.C. §§ 554, 3105. They are all *executive* officers.

501 U.S. at 910 (Scalia, J., concurring in part and concurring in judgment, joined by O'Connor, Kennedy, & Souter, JJ.) (emphasis in original). Justice Breyer has since embraced that same view in his dissent in *Free Enterprise Fund. v. PCAOB*, 561 U.S. 477, 542 (2010) (Breyer, J., dissenting, joined by Stevens, Ginsburg, & Sotomayor, JJ.) ("As Justice Scalia has observed, 'administrative law judges (ALJs) are all executive officers.'").

Like the STJs held to be inferior officers in *Freytag*, the SEC's ALJs all occupy an office that is "established by law," exercise "significant authority" under federal law, and perform more than ministerial tasks in both overseeing and adjudicating myriad administrative proceedings. They also may render final decisions. For these

reasons, the SEC's ALJs are executive officers for Article II purposes.

B. The SEC's ALJs Are *Not* Mere Employees

Insisting that the SEC's ALJs are mere low-level "employees" and not "Officers of the United States," the panel below concluded that holding a hearing before an SEC ALJ is both constitutional and proper. Neither contention is true.

In reaching its conclusion, the appeals court failed even to recite the applicable statutory language that serves as the basis for the SEC's hearing below, § 12 of the Investment Advisers Act. That provision, entitled "Hearings," expressly states that "Hearings ... may be held before the Commission, any member or members thereof, or *any officer or officers of the Commission designated by it* ...." 15 U.S.C. § 80b-12 (emphasis added). Nor is the Investment Advisers Act alone in requiring that hearings be conducted either by the SEC or by "any other officer or officers of the Commission designated by it." Every major statute the SEC enforces has substantially the same language. *See* 15 U.S.C. § 78v (Securities Exchange Act of 1934); 15 U.S.C. § 77u (Securities Act of 1933); 15 U.S.C. § 80a-40 (Investment Company Act of 1940).

On its face, this statutory language confirms that only someone who is an officer of the SEC may hold hearings. And the fact that a hearing officer is statutorily interchangeable with either the SEC itself or a commissioner of the SEC confirms that a hearing officer is someone who enjoys the broad

discretion of an executive officer—one who is empowered to "exercise significant authority pursuant to the laws of the United States." *Free Enter. Fund*, 561 U.S. at 486 (citing *Buckley*, 424 U.S. at 126).

The statutory language is instructive because, until recently, the SEC has interpreted it in a way that allows the SEC's ALJs to exercise significant investigatory powers as "officers" of the SEC—*not* "employees." For example, the SEC's own enforcement manual designates as "senior officers" those who may "administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of documents and other materials" during formal investigative proceedings. *See* SEC Office of Chief Counsel, Enforcement Manual § 2.3.4 (June 4, 2015).

Nonetheless, the D.C. Circuit concluded that SEC ALJs are employees under its prior holding in *Landry v. FDIC*, which held that the FDIC's ALJs were not executive officers. But in reaching that conclusion, the panel misconstrued its own circuit precedent. As the Solicitor General explained in opposing Landry's petition for certiorari, *Landry* "did not purport to establish any categorical rule that administrative judges are employees rather than 'inferior officers.'" U.S. Br. Opposing Cert., *Landry v. FDIC*, No. 99-1916, 2000 WL 34013905, at *7 (U.S. Aug. 28, 2000). Rather, *Landry*'s holding was narrowly limited to evaluating the particular role and duties of only the FDIC's ALJs.

Nor should this Court accept the appeals court's mischaracterization of *Freytag* as somehow

turning on whether an STJ could render a final decision of the Tax Court. On the contrary, as Judge Randolph emphasized in his concurrence in *Landry*, *Freytag* designated the potential finality of an STJ's decision as another, *alternative* basis for its holding that STJs were officers. *See* 204 F.3d at 1142 (Randolph, J., concurring in part and concurring in judgment) (explaining that *Freytag* "clearly designated [an STJ's power to render a final decision] as an alternative holding" to the "conclusion it had reached in the preceding paragraphs—namely ... [STJs] are nevertheless inferior officers of the United States"). In any event, as shown above, *un*like the FDIC's ALJs at issue in *Landry*, the SEC's ALJs may (and often do) render final decisions of the SEC.

Simply put, this Court has *never* held that an individual with federal adjudicative authority is a mere "employee." Instead, the Court has consistently found federal officials with quasi-judicial functions to be "Officers." *See, e.g.*, *Edmond v. United States*, 520 U.S. 651 (1997) (judges of the Coast Guard Court of Criminal Appeals); *Weiss v. United States*, 510 U.S. 163 (1994) (military judges); *Go-Bart Importing Co. v. United States*, 282 U.S. 344 (1931) (United States commissioners), *abrogated on other grounds as stated in Arizona v. Gant*, 556 U.S. 332 (2009).

The SEC's discretion to review the decisions of its ALJs does not change the fact that ALJs are inferior constitutional officers. As the governing statutes and regulations make clear, the SEC's ALJs carry out "important functions," *Freytag*, 501 U.S. at 882, and "exercis[e] significant authority pursuant to

the laws of the United States," *Buckley*, 424 U.S. at 126. Thus, their exercise of authority outside the strictures of the Appointments Clause is *ultra vires*.

II. THE COURT SHOULD ADOPT A REMEDY COMMENSURATE WITH THE GRAVITY OF THE CONSTITUTIONAL VIOLATION

Likely in anticipation of defeat here, the SEC has taken steps to minimize the impact of that defeat on past and present enforcement proceedings still subject to judicial review. In its November 30, 2017 Ratification Order, the SEC sought "[t]o put to rest any claim" that its administrative proceedings were being conducted in violation of the Appointments Clause by

> (1) purporting to "ratif[y] the agency's prior appointment" of the agency's Chief ALJ and its four other ALJs;[2]
>
> (2) directing ALJs, in all pending proceedings in which no initial decision had issued, to "reconsider the record" and decide whether "to ratify or revise in any respect" all prior actions taken by an ALJ in the proceeding; and
>
> (3) remanding all matters still pending before the SEC in which an ALJ has issued an initial decision back to that

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[2] Those whose appointments the SEC purportedly ratified include Cameron Elliot, the ALJ who presided over the enforcement proceedings against petitioners.

> same ALJ to conduct a review of the sort outlined in No. 2 above.

Ratification Order at 1-2.

The Ratification Order did not address this or any of the 13 cases then pending in federal appeals court on petitions for review of SEC enforcement actions. One can reasonably assume, however, that if this Court determines that the SEC appointed its ALJs in violation of the Appointments Clause and lower courts remand those 13 cases back to the agency, the SEC is likely to respond by extending its Ratification Order to all of those cases. Above all, the Ratification Order is reasonably read as a blueprint for how the SEC intends to deal with every adversary proceeding conducted by an unconstitutionally appointed officer.

WLF respectfully suggests that this Court's case law bars any such effort to salvage administrative hearings conducted by officials appointed in violation of the Appointments Clause. WLF urges the Court to address the propriety of the SEC's likely salvage operation now, rather than allow the issue to drag on for several more years—particularly because this precise issue is almost certain to return to the Court. Regardless of the name that government officials have previously used when upholding proceedings conducted by improperly appointed officials—whether the *de facto* officer doctrine, harmless error analysis, or ratification—the Court has uniformly rejected such efforts when (as here) the defendant has raised a timely objection to the qualifications of the presiding officer. The Court should rule that any enforcement

proceedings conducted before an improperly appointed ALJ are a nullity, and that the SEC must start from scratch if it chooses to renew enforcement efforts against the targets of those proceedings.

A. This Court Has Uniformly Rejected Efforts to Salvage Actions Undertaken by Improperly Appointed Officials

During a nine-day hearing conducted as part of the enforcement action against petitioners, ALJ Elliot presided over witness testimony and made rulings not only on the admissibility of evidence and objections to testimony but on the merits of the SEC's charges. Pet. App. 115a-237a. The SEC's Ratification Order makes clear that the SEC wishes to avoid having to conduct new hearings if this Court determines that it improperly appointed its ALJs. It seeks instead to retroactively validate those hearings, provided only that a properly appointed ALJ has reviewed the administrative record and has determined that the proceedings were conducted properly. But this Court has consistently rejected such salvage operations, concluding that endorsing them would undermine compliance with constitutional norms and discourage litigants from even raising meritorious objections to the qualifications of the presiding officer.

Thus, in *Ryder v. United States*, 515 U.S. 177 (1995), the Court unanimously overturned the defendant's conviction by a court-martial on drug charges because one of the courts that reviewed that conviction—the Coast Guard Court of Military Review—included two judges appointed in violation

of the Appointments Clause. The United States conceded the constitutional violation, and the Court rejected each of the Government's many arguments for why the conviction should stand despite that violation. The Court held that application of the *de facto* officer doctrine was limited to a defense against *collateral* attacks on the judgment; it noted that Ryder had challenged the composition of the Coast Guard Court of Military Review "while his case was pending before that Court on direct review." 515 U.S. at 182.

In rejecting the Government's no-harm-no-foul argument, the Court stressed the importance of Article II's requirement that the functions of "Officers" of the United States be reserved for those properly appointed under the Appointments Clause:

> [Ryder's] claim is based on the Appointments Clause of Article II of the Constitution—a claim that there has been a trespass upon the executive power of appointment, rather than a misapplication of a statute. ... We think that one who makes a timely challenge to the constitutional validity of the appointment of an officer who adjudicates his case is entitled to a decision on the merits of the case. ... Any other rule would create a disincentive to raise Appointments Clause challenges with respect to questionable judicial appointments.

Id. at 182-83 (citations omitted). Nor did the Court adopt the Government's suggestion to excuse the

violation because the conviction was later ratified by another (and properly constituted) appellate court—the Court of Military Review, which upheld the conviction in every respect and found the violation of the Appointments Clause to be harmless error. *Id.* at 186-88.[3]

The Court relied on *Ryder* in *Nguyen v. United States*, 539 U.S. 69 (2003), to overturn the judgment of a three-judge Ninth Circuit panel, one of whose members was not an Article III judge. While stating that the *de facto* officer doctrine is sometimes a basis for overlooking "merely technical defects" in the qualifications of a presiding officer, 539 U.S. at 77, the Court held that permitting a non-Article III judge to sit on an Article III court was no mere technical violation: "Congress' decision to preserve the Article III character of the courts of appeals is more than a trivial concern ... and is entitled to respect." *Id.* at 80. The Court rejected the Government's argument that the judgment should be upheld because the proceedings were fair and the votes of the panel's two Article III judges were enough to ratify the judgment. *Id.* at 80-83. Instead, the Court ordered a "fresh consideration" of the appeal by "a properly constituted panel." *Id.* at 83.[4]

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[3] The Court recognized that the *de facto* officer doctrine may be relevant when the voiding of all *ultra vires* decisions by an unauthorized officer might lead to a massive disruption of government operations. But the Court held that such concerns did not arise in Ryder's case given the limited number of cases on direct review (between 7 and 10) implicated by the Court's decision. *Id.* at 185-86.

[4] The D.C. Circuit recently relied on *Nguyen* to hold that the actions of the Acting General Counsel of the NLRB

Similarly, in *Glidden Co. v. Zdanok*, 370 U.S. 530 (1962), the Court concluded that federal court judgments[5] could not stand if issued by judges not appointed in accordance with Article III of the Constitution. The Government argued that even if the challenged judges were serving improperly in Article III federal courts, the judgments should survive under the *de facto* officer doctrine.

Writing for the Court, Justice Harlan rejected that contention. 370 U.S. at 535-37. While acknowledging that the *de facto* officer doctrine might "immunize from examination" a "defect in statutory authorization for a particular intracircuit assignment" of a federal judge, the Court held that the doctrine could not save proceedings presided over by an official appointed in violation of constitutional norms:

> The alleged defect of authority here relates to basic constitutional protections designed in part for the benefit of litigants. ... It should be

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(whose appointment violated the Appointments Clause and the Federal Vacancies Reform Act) could not be salvaged based on either harmless error or the *de facto* officer doctrine. *SW General, Inc. v. NLRB*, 796 F.3d 67, 79-82 (D.C. Cir. 2015), *aff'd*, 137 S. Ct. 929 (2017). The appeals court found that *Nguyen* precluded any application of the *de facto* officer doctrine to an Appointments Clause defect. *Id.* at 81.

[5] One of the judgments (from the Second Circuit) was by a three-judge panel that included a judge from the Court of Claims sitting by designation. The other judgment (from the U.S. District Court for the District of Columbia) was by a retired judge of the Court of Customs and Patent Appeals.

> examinable *at least on direct review*, where its consideration encounters none of the objections associated with the principle of res judicata, that there be an end to litigation.

Id. at 536 (emphasis added).[6] Significantly, the Court has never given effect—in any guise—to an adjudicatory action by an unconstitutional official.

B. Merely Assigning a New Name to Efforts to Salvage Prior Proceedings Is Insufficient to Distinguish *Ryder* and *Nguyen*

Perhaps recognizing that the Government has fared poorly before this Court when it has tried to invoke the *de facto* officer doctrine and harmless error analysis to rescue *ultra vires* proceedings before improperly appointed officials, the SEC has resorted to a change in nomenclature. Its Ratification Order asserts that newly minted ALJs may "ratify" proceedings conducted (it apparently fears) in violation of the Appointments Clause. That change in wording, however, cannot permit the SEC to salvage federal adjudicatory proceedings by unconstitutionally appointed officials. An agency is, of course, permitted to "ratify" past actions in the sense that it may renew its enforcement actions in a timely manner. But this Court has *never* upheld Executive-Branch ratification of administrative actions that

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[6] The Court ultimately concluded that the two judges sitting by designation were, in fact, Article III judges, and so it affirmed the judgments below solely on that basis. *Id.* at 584.

were *ultra vires* when undertaken.

The Government has sought such ratification in this Court only once, and the Court overwhelmingly rejected that effort. *FEC v. NRA Political Victory Fund*, 513 U.S. 88 (1994). In that case, the Government was not even seeking to ratify an entire administrative proceeding; it merely sought to ratify the filing of a certiorari petition by a federal agency (the Federal Election Commission) that lacked the independent litigating authority to file such a petition on its own.

The Court explained that any effort to ratify prior unauthorized government action is limited by the longstanding agency-law principle that "the party ratifying should be able not merely to do the act ratified at the time it was done, but also at the time the ratification was made." *Id.* at 98 (emphasis omitted) (quoting *Cook v. Tullis*, 85 U.S. 332, 338 (1873)). Because the Government's purported ratification did not meet that standard, the Court dismissed the certiorari petition. *Id.* at 99.

NRA Political Victory Fund is fatal to any SEC effort to distinguish *Ryder* and *Nguyen* by characterizing its attempt to excuse its unconstitutional ALJ proceedings as a "ratification" of those proceedings. If petitioners prevail on the merits of their Appointments Clause challenge, it will be uncontested that the SEC's five ALJs lacked authority "to do the act ratified at the time the act was done." Those ALJs received that authority no earlier than November 30, 2017, when the SEC

issued its Ratification Order.[7] Indeed, the SEC lacked *any* ALJs who were constitutionally authorized to conduct enforcement proceedings against petitioners at the time ALJ Elliot conducted his nine-day hearing in 2013. Without that authority, newly appointed ALJs are barred by *NRA Political Victory Fund* from ratifying proceedings conducted by improperly appointed ALJs.[8]

In several cases, the Court has permitted *Congress* to ratify Executive Branch acts undertaken by officials unauthorized to act, but only if Congress *was* so authorized to act at the time of the initial act. *See, e.g., United States v. Heinszen*, 206 U.S. 370 (1907) (holding that although a Presidential order imposing a duty on Philippines-bound goods was unauthorized when first issued, legislation enacted in 1902 by Congress—*which could have imposed the same duty via legislation at the time of the initial Presidential order*—served to ratify the order). But in none of those cases did the Court uphold

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[7] Petitioners mount a strong argument that even the Ratification Order does not satisfy the Appointments Clause's requirements for appointing the five ALJs as "Officers" of the United States. Pet. Br. 50-51.

[8] This Court's ratification rule is consistent with the Restatement (Third) of Agency § 4.05 (2006): "A ratification of a transaction is not effective unless it *precedes* the occurrence of circumstances that would cause the ratification to have adverse and inequitable effects on the rights of third parties" (emphasis added). As third parties to any purported ratification, petitioners will suffer serious adverse effects if the SEC may ratify its 2013 proceedings by an unconstitutional official: they will be subject to a ruinous order that directly resulted from *ultra vires* acts.

ratification by *the Executive Branch*, and none involved ratification of adjudicative proceedings before an administrative agency or court.[9] Indeed, *Heinszen* explicitly limited ratification to events *preceding* a substantive court ruling in legal proceedings arising out of the prior Executive Branch action. *See* 206 U.S. at 387-88.

C. The Court Should Reach the Ratification Issue Now, Rather than Remanding the Case and waiting Its Inevitable Return to This Court

Petitioners have shown that the SEC has acted unconstitutionally by seeking to impose sanctions on them based on administrative proceedings conducted by an official who was not (but should have been) appointed consistent with the Appointments Clause. Petitioners are therefore entitled to a remedy that is commensurate with the gravity of that constitutional violation. Merely vacating the SEC's action and directing the agency to begin anew is not an adequate remedy. By issuing its Ratification Order, the SEC has made clear that—if this matter is merely vacated and remanded—it intends to send this matter back to

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[9] Congress has also expressed its disapproval of ratification of agency decisions by Executive Branch officials through the Federal Vacancy Reform Act of 1998 (FVRA). The FVRA provides that, with rare exceptions, actions taken by officials improperly appointed to federal vacancies "shall have no force and effect" and "may not be ratified." 5 U.S.C. § 3348(d).

ALJ Elliot to permit him to salvage the prior proceedings by declaring them "ratified."[10] As explained above, however, any such effort to salvage the prior proceedings is constitutionally impermissible.

To forestall the SEC's anticipated conduct that would compound the agency's constitutional violations, an appropriate remedy is to (1) vacate all SEC actions undertaken against petitioners to date (including the Commission's decision to refer charges to a hearing before an unauthorized official);[11] and (2) direct the agency that if it wishes to proceed against petitioners, it must file new, timely charges. Anything less would render petitioner's victory Pyrrhic and make it highly likely that the case will

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[10] WLF notes that the consistent pattern of the SEC's ALJs, in the wake of the November 30, 2017 Ratification Order has been to declare that they are now duly appointed Officers (without conceding any defect in their prior status) and that they may ratify their own prior rulings and proceedings in toto. *See, e.g., In the Matter of David Pruitt, CPA*, Admin. Proceeding File No. 3-17950, Order Denying Motion for Stay (February 15, 2018).

[11] The vacated actions should include not only all proceedings before ALJ Elliot but also the Commission's September 5, 2012 order instituting proceedings against petitioners. That order suffers from the same constitutional defect as the later proceedings before ALJ Elliot because it explicitly directed that proceedings be conducted before an official that the Commission knew was not appointed consistent with the Appointments Clause. *See* September 5, 2012 Order at 10 ("It is ordered that a public hearing for the purpose of taking evidence on the questions set forth in Section III shall be convened ... before an Administrative Law Judge to be designated by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.").

return to this Court in several years.

A remedy of that nature is particularly warranted because the initial petition for review from any "ratified" SEC enforcement order would be to the D.C. Circuit, and that Court has issued several problematic decisions that have mistakenly adopted a doctrine that affords federal agencies broad authority to ratify their prior *ultra vires* actions. So without a meaningful remedy, petitioners will likely be forced to return to this Court for relief from the SEC's anticipated ratification decision.

The D.C. Circuit recognized the right of federal agencies to ratify prior, *ultra vires* actions in the immediate aftermath of its decision in *NRA Political Victory Fund*, which held that having two congressional officers serve as members of the FEC violated the Constitution and required the invalidation of actions taken by that improperly constituted body. *FEC v. NRA Political Victory Fund*, 6 F.3d 821 (D.C. Cir. 1993), *cert. dism'd*, 513 U.S. 88 (1994). The reconstituted FEC then voted to ratify the "old" FEC's decision to file a civil enforcement action against Legi-Tech, Inc., a company that marketed computer database services. The D.C. Circuit upheld the FEC's ratification decision without even citing, let alone trying to distinguish, this Court's *NRA Political Victory Fund* decision (which had rejected the Government's ratification efforts and dismissed as untimely the FEC's petition for review of the D.C. Circuit's decision). *FEC v. Legi-Tech, Inc.*, 75 F.3d 704 (D.C. Cir. 1996).

Legi-Tech's "ratification" was limited to an

initial FEC decision to file a federal-court lawsuit, not (as will likely be the case here) ratification of an entire *ultra vires* administrative proceeding. But a later D.C. Circuit decision expanded *Legi-Tech* and held that the appeals court's ratification doctrine does, indeed, apply that broadly. *See Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd.*, 796 F.3d 111 (D.C. Cir. 2015). In *Intercollegiate*, the appeals court held: (1) the composition of the Copyright Royalty Board, a federal agency that determines royalty rates for webcasting, was unconstitutional (because members were appointed in violation of the Appointments Clause); (2) the royalty rates established by the "old" board were therefore invalid; but (3) a reconstituted board (whose members were constitutionally appointed) could "ratify" the royalty-rate decision of the "old" board based on the written record compiled by the "old" board, without conducting a new hearing. 796 F.3d at 118-121. The Court deemed it irrelevant that, in setting royalty rates, the board was "exercis[ing] judicial authority in an adversarial proceeding" and yet was relying on a paper record compiled by an administrative body unauthorized to act. *Id.* at 119.

Intercollegiate found it appropriate to impose at least some constraints on the authority of an agency to "ratify" the *ultra vires* actions of an earlier entity. The appeals court held that the ratifier's reconsideration must entail something more than a mere rubber-stamp of the previous actions: it limited ratification to situations in which "a properly appointed official has the power to conduct an independent evaluation of the merits *and does so*." *Id.* at 117 (emphasis added).

But the D.C. Circuit has since abandoned even that modest check on ratification authority. In *Wilkes-Barre Hospital Co. v. NLRB*, 857 F.3d 364 (D.C. Cir. 2017), the appeals court upheld an NLRB Regional Director's ratification of his own prior, invalid decision to begin and prosecute Unfair Labor Practice (ULP) proceedings against the petitioner.[12] The court declined to examine the petitioner's claim that the Regional Director had not carefully considered the whole record before ratifying his decision to prosecute ULP claims against the petitioner, stating that "even if the subsequent review was nothing more than a rubberstamp, it resolved any Appointment Clause deficiencies." *Id.* at 372 (citations omitted).

As shown above, the D.C. Circuit's entire line of "ratification" decisions misreads this Court's case law. The ratification endorsed by the D.C. Circuit conflicts with this Court's *NRA Political Victory Fund* decision and is indistinguishable from the *de facto* officer doctrine roundly rejected by *Ryder* and *Nguyen*. In *Ryder*, the Court rejected the Government's argument that the judgment of the Coast Guard Court of Military Review, although rendered invalid because two of the court's five members were appointed in violation of the Appointments Clause, could be ratified by the properly constituted Court of Military Appeals (which held that the error of the lower appeals court was harmless). *Ryder*, 515 U.S. at 186-88. In

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[12] All parties agreed that, at the time of the initial decision, the Regional Director's appointment had not complied with the Appointments Clause.

Nguyen, the Court rejected arguments that the presence of two validly appointed Article III judges on the Ninth Circuit panel was enough to overcome the taint created by the improper third panel member. *Nguyen*, 539 U.S. at 83-84.

A principal concern animating *Ryder*—that overlooking the Appointments Clause in that case would create an inappropriate "disincentive to raise Appointments Clause challenges with respect to questionable judicial appointments," 515 U.S. at 183—is equally applicable to the SEC's efforts to ratify proceedings before unconstitutionally appointed ALJs. Moreover, as in *Ryder* and *Nguyen*, the Court need not worry that a decision preventing ratification of the SEC's *ultra vires* proceedings would cause administrative chaos within the Government; the number of SEC enforcement actions that are on direct review—and thus potentially affected by a no-ratification decision—is quite small.

Finally, WLF shares petitioners' concern over the unseemliness of returning remanded proceedings to the same official who (as an unauthorized ALJ) ruled against the defendant and imposed sanctions. Even if the ALJ, following confirmation of his status as an Officer of the United States, were obliged to conduct brand new proceedings, human nature suggests that any such ALJ would be sorely tempted to conclude that his original, constitutionally unauthorized handling of the proceedings was eminently fair and to issue the very same rulings he issued in the initial proceedings. For these reasons, WLF respectfully suggests that the Court's remedy include an order directing that any renewed

proceedings must be conducted by someone other than ALJ Elliot.

CONCLUSION

For the foregoing reasons, the judgment below should be reversed.

Respectfully submitted,

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Supreme Court of the United States

RAYMOND J. LUCIA

Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF *AMICUS CURIAE* DAVID ZARING IN SUPPORT OF RESPONDENT

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INTEREST OF *AMICUS CURIAE*

Amicus David Zaring is associate professor at the Wharton School of the University of Pennsylvania. He is a scholar of financial regulatory institutions, and has written in particular about the Securities and Exchange Commission's administrative proceedings program challenged in this case. He has no financial or other interest in this case.[1]

[1] This brief is filed pursuant to consents obtained from all parties. No person other than amicus and his counsel have authored this brief in whole or in part or made a monetary contribution toward its preparation or submission.

SUMMARY OF THE ARGUMENT

Congress has encouraged agencies to formulate policy through formal adjudication since the passage of the Administrative Procedure Act ("APA") in 1946. 5 U.S.C. §§ 551-559, 701-706, 1305, 3105, 3344, 4301, 5335, 5372, 7521. This brief reports on a comprehensive study of how formal adjudication has worked at the Securities and Exchange Commission ("SEC") in the five years since the passage of the Dodd-Frank Wall Street Reform Act of 2010, which broadened the reach of administrative proceedings. That study offers two findings that should reassure the Court that the process Congress created in the APA is functioning well at the SEC.

First, the agency's Administrative Law Judges ("ALJs") function as impartial decision-makers that serve the Commission, but do not overly influence its resolution of contested cases. Commissioners accept ALJ recommendations in such cases approximately half of the time. This suggests that while SEC ALJs serve the agency by building a factual and legal record designed to improve the quality of agency policymaking, the Commission's review of this record is just as searching and careful. The study establishes that the Commission is both the de facto and de jure final word in administrative proceedings. *See* David Zaring, *Enforcement Discretion at the SEC*, 94 Tex. L. Rev. 1155, 1184–85 (2016).

Second, a quantitative and qualitative analysis of SEC proceedings, paired with a comparison to the record of securities defendants in judicial proceedings in the Southern District of New York, shows that the SEC does not enjoy more favorable outcomes in front of ALJs than it does in front of

Article III judges. *See id.* at 1185–89. Instead, ALJs regularly rule against the agency; there is no home-court advantage when it comes to administrative proceedings.

A pillar of the administrative state, SEC ALJs serve politically accountable commissioners by supervising high-quality administrative proceedings. The Court should resist finding that the appointment of ALJs constitutes a technical violation of the Appointments Clause.

ARGUMENT

I. The SEC's ALJs merely carry out the policies of politically accountable agency heads.

The APA carves out a role for ALJs not as an independent judiciary, but as fair and impartial decision-makers that serve the agency by building a factual record that can be used to effectuate the agency's policies and objectives. Indeed, the outcome of ALJ decision-making rests in the hands of the agency commissioners, who need not, and do not, grant the ALJ's fact-finding or legal conclusions the respect of finality or even deference. *See* Paul R. Verkuil, *Reflections upon the Federal Administrative Judiciary*, 39 UCLA L. Rev. 1341, 1353 (1992). The APA provides that "[o]n appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision." 5 U.S.C. § 557(b). Congress has directed the *agency*, not the ALJ, to interpret gaps in statutes and regulations, and to formulate policy through the process of formal adjudication. *See* Harold J. Krent

& Lindsay DuVall, *Accommodating ALJ Decision Making Independence with Institutional Interests of the Administrative Judiciary*, 25 J. Nat'l Ass'n Admin. L. Judges 1, 29 (2005). As a result, every decision made by an SEC ALJ is reversible by the commissioners themselves, who subject those decisions to *de novo* review as a matter of law, and to searching evaluation (as expressed in lengthy opinions) as a matter of practice.

Certainly the APA fosters a certain amount of independence for administrative judges as a means toward impartial decision-making, and to ensure that the administrative judiciary is not captive to special interests. *See* James E. Moliterno, *The Administrative Judiciary's Independence Myth*, 41 Wake Forest L. Rev. 1191, 1215 (2006) (explaining that the original Administrative Procedure Act's legislative history shows that Congress intended administrative judges to "conduct themselves in the manner in which people think they should—that is, as judges and not as the representatives of factions or special interests" (citing 92 Cong. Rec. 5, 5650 (1946)).[2] But the APA does not afford ALJs independence from the members of the executive branch which they serve. Congress considered and

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[2] The federal government has always worried about making its administrative adjudicators too politically accountable—and the poor record of patronage and other problems surrounding the federal hearing examiners who were replaced by ALJs underscores the weaknesses of agency judges whose appointments often reflected a degree of patronage. *See generally* Morgan Thomas, *The Selection of Federal Hearing Examiners: Pressure Groups and the Administrative Process*, 59 Yale L.J. 431 (1950) (reviewing the skepticism administrative lawyers had of pre-APA hearing examiners, and recording the large numbers dismissed from the civil service upon passage of the statute).

rejected the possibility that ALJs could be given real independence from the agency when it chose to locate appeals from ALJ decisions to the agency heads for whom they work, rather than to a centralized panel of administrative adjudicators. *See* Moliterno, *supra*, at 1227.

Under the APA's system of administrative adjudication, agency heads, not ALJs, make policy; ALJs act as impartial decision-makers and advancers of agency policy. *See id.* at 1211. As one ALJ has observed, ALJs "act on behalf of those agencies," and therefore "are often expected to help achieve agency objectives." Edwin L. Felter, Jr., *Maintaining the Balance Between Judicial Independence and Accountability in Administrative Law*, Judges' J., Winter 1997, at 22, 22. Ultimately, the agency's action is the responsibility of its politically accountable commissioners.

We can get a sense of the quantity and quality of Commission review under 5 U.S.C. § 557(b) by examining the Commission's review of initial decisions decided between December 2010 and December 2015. Excluding ministerial affirmances (affirmances based on the respondent's failure to make or perfect an appeal), Commission review of the remaining cases is quite searching and lengthy, almost always including a statement of facts, a legal analysis, and an evaluation of the appropriate form of relief, none of which are cribbed from the ALJ's initial decision. One of the incantations of the commissioners, repeated at the beginning of many of their decisions, is that their decision would be based on an "independent review of the record."[3]

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[3] Of the 197 initial decisions reviewed by the Commission over five years, forty-seven included the phrase "independent review

I identified fifty-five cases where the Commission made a substantive decision during the five year period after the passage of Dodd-Frank.[4] In twenty-nine of those decisions, the Commission affirmed the ALJ's initial decision. In eight decisions, the Commission affirmed the decision directionally, but modified the remedy. In eighteen cases, the Commission reversed the ALJ's decision. Overall, in those cases where the Commission completed its review, it reversed or modified the initial decision only slightly less than half of the time.

While the Appointments Clause is designed to make the President accountable to the electorate in appointing officers of the United States, including agency heads, the role of the administrative judiciary is to serve the executive branch and to administer the policies created by agency heads. *See* Moliterno, *supra*, at 1217. As such, the Court need not destabilize an enforcement channel that has been a part of the SEC since its founding,[5] and with

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of the record" and others included phrases like it. *SEC Commission Opinions & Orders Search*, BLOOMBERG L., https://www.bloomberglaw.com/legal_search (follow "Search & Browse" hyperlink, then "All Legal Content;" then search keywords "'initial decision' & 'independent review of the record'" and modify search criteria for source "SEC Commission Opinions & Orders" and date range 12/08/2010 to 12/08/2015).

[4] As I have noted, the review began with decisions issued in December 2010, five months after the passage of the statute, on the assumption that the agency was unlikely to change its policies so soon after promulgation.

[5] Prior to the APA's passage (and after it), the agency's adjudicators were called "hearing examiners," a term that was changed in 1978. Roger C. Crampton, *Title Change for Federal Hearing Examiners? "A Rose By Any Other Name...,"* 40 Geo. Wash. L. Rev. 918, 922 (1972) (the "title 'examiner' has long

the administrative state for as long as it has been governed by the APA.

II. A quantitative study of recent administrative proceedings establishes that defendants do not fare better before judges than before ALJs.

This brief reports on a study of the initial decisions of ALJs since the passage of Dodd-Frank through early 2015 and analyzes the 358 initial judgments issued over that period, both quantitatively (in this section) and qualitatively (in the next section), to see what they can reveal about administrative proceedings. *See* Zaring, *supra*, at 1185–89.

It could be the case that the matters brought before the ALJs enjoy a strong home-court advantage, and further, it could be the case that the experiences for defendants would differ between federal court and administrative proceedings.

But outcomes—and some aspects of the administrative process as well—can be examined with data.

The SEC's success rate varied from year to year. For instance, in fiscal year 2014, the SEC won every administrative case that went to a judgment, including all fourteen cases that went to trial. Jenna Greene, *The SEC's on a Long Winning Streak: Criticism Rises over the Agency's In-House Forum*,

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been used by federal administrative agencies, even before the present role of the APA examiner was established"); Pub. L. No. 95-251, 92 Stat. 183, 183-84 (1978) (substituting "administrative law judge" for "hearing examiner").

Nat'l L.J. (Jan. 19, 2015).[6] The SEC has not been uniformly successful in the administrative realm, however, comprehensively losing cases in the administrative forum in 2011,[7] three times in 2013,[8] and once in 2015.[9] Moreover, most of the ALJs who work at the SEC have ruled against the agency in the last two years.

Indeed, the SEC does not enjoy more favorable

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[6] https://www.law.com/nationallawjournal/almID/1202715464297/the-secs-on-a-long-winning-streak/. By contrast, in 2014, the SEC conducted seventeen federal court trials and lost seven. Bruce Carton, *SEC Riding Lengthy Unbeaten Streak in Administrative Proceedings*, Compliance Wk. (Jan. 20, 2015), https://www.complianceweek.com/blogs/enforcement-action/sec-riding-lengthy-unbeaten-streak-in-administrative-proceedings.

[7] *See In re* John P. Flannery, Initial Decision Release No. 438, 2011 SEC LEXIS 3835 (ALJ Oct. 28, 2011) ("*In re* John P. Flannery") (finding no violation of securities laws after a lengthy administrative hearing where the SEC alleged material misstatements to shareholders); Alison Frankel, *SEC Loses Again: Agency Judge Clears State Street Execs*, Reuters (Oct. 31, 2011), https://perma.cc/NYK9-DVHE (summarizing the *Flannery* decision).

[8] *In re* Miguel A. Ferrer, Initial Decision Release No. 513, 2013 WL 5800586, at *83 (ALJ Oct. 29, 2013); *In re* S.W. Hatfield, Initial Decision Release No. 504, 2013 WL 4806917, at *4 (ALJ Sept. 10, 2013), *rev'd*, Exchange Act Release No. 73,763, 2014 WL 6850921 (Dec. 5, 2014); *In re* Jilaine H. Bauer, Initial Decision Release No. 483, 2013 SEC LEXIS 1125 (ALJ Apr. 16, 2013).

[9] *In re* Thomas R. Delaney II, Initial Decision Release No. 755, 2015 WL 1223971, at *61 (ALJ Mar. 18, 2015) (finding no supervisory liability for one respondent in a Rule 204 case that went to administrative hearing); *see also* Aruna Viswanatha, *Amid Cries of Home Field Advantage, SEC Loses Case in In-House Court*, Wall Street J. Moneybeat (Mar. 19, 2015, 2:15 PM), https://blogs.wsj.com/moneybeat/2015/03/19/amid-cries-of-home-field-advantage-sec-loses-case-in-in-house-court/ (providing a detailed account of how "the [SEC] lost part of its case" before an SEC ALJ).

outcomes in front of its ALJs than it does in front of Article III judges. The agency only received all the remedies it sought in 71% of the initial decisions in the five year period I studied. That is not too different than the rule-of-thumb rate for victories by any federal agency in federal court which, when various studies are pooled, comes out to about 69%. David Zaring, *Reasonable Agencies*, 96 Va. L. Rev. 135, 170 (2010).

The cases brought in the Southern District of New York during the period where the SEC brought enforcement claims against defendants are revealing. The Southern District of New York ("SDNY"), which covers Manhattan, is ground zero of securities enforcement in the federal courts. The court is composed of judges with experience in securities fraud cases, both civil and criminal, some of whom have a reputation for putting the agency through its paces. Of the 119 reported cases in the district, the agency's success rate was high; it received a positive result in 111 of the tracked cases. The cases were almost evenly split between claims brought under the Securities Act of 1933, 15 U.S.C. § 77a (fifty-four of 119 cases), and the Securities Exchange Act of 1934, 15 U.S.C. § 78a (sixty-four cases), and the SEC's rate of success did not particularly differ between the two bodies of law. ALJs write shorter opinions—on average 6,200-word decisions since Dodd-Frank—while the SDNY bench as a whole has averaged 12,500 words. District judges are unlikely to cite administrative proceedings, but ALJs often cite judicial opinions. Zaring, *Enforcement Discretion at the SEC*, *supra*, at 1188-89.

Over the sample period, these results make the

SEC look like a comparably victorious enforcer regardless of the forum in which it chose to pursue enforcement; there is no statistically significant distinction between the rates of success. With eight failures in Manhattan, compared to only six over the enforcement proceedings brought before its ALJs during the same period, there is little evidence that the forum chosen by the SEC resulted in stark advantages for the agency either way.

III. A qualitative review of the administrative proceedings where the SEC lost shows that the agency does not enjoy home-court advantage in administrative proceedings.

Much of what ALJs do is routine: defaulting defendants who fail to respond to complaints, imposing sanctions on brokers and investment advisors who have already been adjudged to commit securities fraud in federal court, and so on.

But agency adjudicators have also heard more complicated insider trading and securities fraud cases for many years, consistent with Congress's decision to expand the sorts of matters that could be brought administratively in 1990 and 2010.[10]

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[10] *See* Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, § 102, 104 Stat. 931, 933 (1990) (codified at 15 U.S.C. § 77h-1) (permitting SEC ALJs to hear claims for disgorgement); Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 929p, 124 Stat. 1376, 1862–65 (2010) (codified in scattered sections of 15 U.S.C.) (expanding the jurisdiction of ALJs to violations of the securities laws by defendants who were not registered by the SEC). The House, though not yet the Senate, has also turned to ALJs to reform the process involved in

A qualitative and legal examination of the cases in which ALJs have heard high-profile cases of first impression, and the context in which they hear them, shows that they treat defendants fairly. Most importantly, they do not always side with the agency. High profile rulings by ALJs against the agency have characterized the years after the financial crisis, including:

- A ruling against the agency's efforts to enforce against one of the few female private equity entrepreneurs for securities fraud. *In re* Lynn Tilton, Initial Decision Release No. 1182, 2017 SEC LEXIS 3051 (ALJ Sept. 27, 2017) ("*In re* Lynn Tilton").
- An insider trading case involving the sale of an Atlanta firm. *In re* Charles L. Hill Jr., Initial Decision Release No. 1123, 2017 SEC LEXIS 1154 (ALJ Apr. 18, 2017).
- A 2011 case against employees of State Street for misleading investors about the extent of subprime mortgage-backed securities held in an unregistered fund. *In re* John P. Flannery. That case set back the SEC's efforts to hold more bankers liable for fraud in the run-up to the financial crisis, and cannot be characterized as a politically popular or supine opinion; indeed, the SEC commissioners themselves, over two dissents, overruled

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promulgating major rules. The Regulatory Accountability Act, H.R. 5 (2017) provides that an "agency shall provide a reasonable opportunity for cross-examination" in compliance "with sections 556 and 557" of the APA for "high-impact rules." The hearings in those sections are ordinarily presided over by ALJs. *See* Regulatory Accountability Act of 2017, H.R. 5, 115th Cong. § 103(e) (2017).

> the opinion on appeal. *In re* John P. Flannery, Opinion of the Commission, Securities Act Release No. 9689, Exchange Act Release No. 73,840, Investment Advisers Act Release No. 3981, Investment Company Act Release No. 31,374, 2014 WL 7145625, at *41–42 (Dec. 15, 2014).

These cases exemplify a willingness of SEC ALJs to decide for defendants in contested cases brought by the agency's enforcement division, and they are not outliers. *See, e.g., In re* Equity Trust Company, Initial Decision Release No. 1030, 2016 SEC LEXIS 2253 (ALJ June 27, 2016) (Foelak); *In re* Donald F. ("Jay") Lathen, Jr., Initial Decision Release No. 1161, 2017 SEC LEXIS 2509 (ALJ Aug. 16, 2017) (Patil); *In re* Med-X, Inc., Initial Decision Release No. 1130, 2017 SEC LEXIS 1347 (ALJ May 8, 2017) (Patil); *In re* RAHFCO Management Group, LLC, Initial Decision Release No. 1047, 2016 SEC LEXIS 2807 (ALJ Aug. 16, 2016); *In re* The Robare Group, Ltd., Initial Decision Release No. 806, 2015 SEC LEXIS 2248 (ALJ June 4, 2015) (Grimes).

In the September 2017 Lynn Tilton case, for example, SEC ALJ Carol Fox Foelak ruled in favor of the defendant, the manager of a variety of distressed private equity funds. *In re* Lynn Tilton. Ms. Tilton had waged a long legal fight to have her case heard in federal court rather than in front of an ALJ, claiming that the agency's administrative process was unfair. Bob Van Voris & Matt Robinson, *Lynn Tilton Wins SEC Fraud Trial She Worked Hard to Avoid*, Bloomberg (Sept. 27, 2017), https://www.bloomberg.com/news/articles/2017-09-27/lynn-tilton-wins-sec-trial-she-d-worked-hard-to-avoid. She was charged with violating various anti-

fraud provisions of the Investment Advisers Act by collecting unearned fees, not disclosing conflicts of interest, and issuing false and misleading financial statements in connection with her firm's operation of three collateral loan obligation funds. The ALJ in the case found that all of the alleged violations were unproven and ordered the proceeding dismissed. *In re* Lynn Tilton.[11]

Of course, not every case brought before an ALJ is a big one. Although a great deal of attention has been paid to these high-profile cases, the mix of traditional cases to new cases has not changed much in the aggregate. Of the SEC's 610 administrative proceedings initiated in 2014, more than half of them were in three categories: "[b]roker-[d]ealer," "[d]elinquent [f]ilings," and "[i]nvestment [a]dvisors/[i]nvestment [c]ompanies" cases. U.S. Sec. & Exch. Comm'n, *Select SEC and Market Data: Fiscal 2014*, at 3 (2014) ("SEC Fiscal 2014 Data"), https://www.sec.gov/files/secstats2014.pdf. All three of these areas involve regulated entities that were unaffected by Dodd-Frank's changes to the administrative cease-and-desist proceedings. These are areas where the SEC traditionally brings

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[11] Two other prominent cases where the SEC lost excused defendants charged with failing to supervise their subordinates, both of whom were engaged in work designed to comply with SEC rules. One featured a partner at Ernst & Young; the partner's subordinate was barred from practicing before the SEC for one year, but the partner escaped sanction. *In re* Gerard A.M. Oprins, Initial Decision Release No. 411, 100 SEC Docket 393, 393, 415–16 (ALJ Dec. 28, 2010). In the other, charges against the CEO of a large multinational clearing firm were dismissed for his own failures to supervise his chief compliance officer. *In re* Thomas R. Delaney II, Initial Decision Release No. 755, 2015 WL 1223971, at *1–2, *61 (ALJ Mar. 18, 2015).

comparatively few civil actions in federal court, and there is little reason to think that ALJ supervision of the disputes reflects a newly overreaching agency—they have been part of the routine of administrative proceedings for 30 years.

Once ALJs do hear complicated cases, the opinions they render are organized and lengthy rather than cavalier; they mimic the look and feel of securities law opinions rendered by Manhattan district judges. Initial decisions accordingly follow a pattern. ALJs begin with an overview, continue with a recounting of the facts (sometimes at great length) followed by a turn to the law, which is then applied to the facts. Then, sanctions are discussed (except in the rather rare case where none are imposed), and the discussions conclude with an order. Even the citations are standard: a leading case on the factors to be considered when imposing sanctions, *Steadman v. SEC*, 603 F.2d 1126 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981), was cited in 239 of the 359 opinions in the five year period starting at the end of 2010.

Nor has it mattered, at least when the opinions issued since Dodd-Frank are compared, which ALJ decides which case; no adjudicator was more likely to rule for the SEC than others, at least based on a regression analysis of the five year sample. In the past two years, three of the five ALJs employed by the SEC during my study have ruled against the agency, in a context where the agency is bringing fewer contested cases to its in-house judges. Other empirical studies of the ALJs have also indicated no evidence of bias towards the agency. *See* Urska Velikonja, *Are the SEC's Administrative Law Judges Biased? An Empirical Investigation*, 92 Wash. L.

Rev. 315 (2017); Joseph A. Grundfest, *Fair or Foul: SEC Administrative Proceedings and Prospects for Reform through Removal Legislation*, 85 Fordham L. Rev. 1143, 1178 (2016) ("there is no statistically significant difference between the SEC's success rate before ALJs and its success rate in federal court").[12]

These results are unsurprising, given that SEC ALJs offer defendants elaborate procedural protections and provide trial-like proceedings that result in a complete record on which the Commission can issue its final decision.

ALJs and Article III judges have different roles: the former issue initial decisions that cannot take effect without action (or deliberate inaction) by the Commission, while the latter issue binding final decisions subject only to review by appellate courts. Nevertheless, ALJs conduct hearings "in a manner similar to federal bench trials," giving parties the opportunity to submit briefs, and preparing decisions that contain proposed findings of fact and conclusions of law. *Office of Administrative Law Judges*, U.S. Sec. & Exch. Comm'n, https://www.sec.gov/alj (last visited Mar. 28, 2018).

For example, ALJs have the authority to administer oaths and affirmations to witnesses and oversee the taking of evidence, ruling on questions of admissibility and accepting offers of proof. 17 C.F.R. § 201.111(a), (c). In addition, parties to an SEC ALJ hearing are permitted to conduct depositions (a maximum of three depositions in a single-respondent proceeding and five depositions per side in a multi-

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[12] The best predictors of success against the agency before ALJs lie in the sort of representation that defendants have obtained and whether they are publicly traded companies alleged to have made errors in their public filings.

respondent proceeding, with an additional two depositions if a party can demonstrate a compelling need). *Id.* § 201.233(a).

The SEC's Rules of Practice also impose a *Brady* obligation on the agency—a requirement that it turn over all exculpatory information to the defendant before any hearing. *Brady v. Maryland*, 373 U.S. 83 (1963); 17 C.F.R. § 201.230. The Court has confirmed that procedural protections offered by administrative hearings are comparable to federal district court procedures. *See e.g., Fed. Mar. Comm'n v. S.C. Ports Auth.*, 535 U.S. 743, 757-8 (2002) (comparing the Federal Maritime Commission's Rules of Practice and Procedure with procedures for civil litigation in federal courts); *Butz v. Economou*, 438 U.S. 478, 513 (1978).[13]

As a result, the parties to an SEC administrative proceeding enjoy ample process and an opportunity to fully and fairly litigate the relevant issues, thus providing a thorough record on which a final decision by the Commission can be based.

The picture is in many ways reassuring. ALJs do not, as discussed above, offer a particularly different form of justice than do federal courts, and they do require the SEC Enforcement Division to be

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[13] The Court has held that the fact that proceedings inside an agency were brought before an ALJ indicated that the requirements of due process were satisfied rather than violated. *See, e.g., Marshall v. Jerrico, Inc.*, 446 U.S. 238, 248–52 (1980) (holding that a civil penalty system permitting payment of fines assessed by an administrative law judge to a federal agency did not violate due process because it was "the administrative law judge, not the [Employment Standards Administration], who performs the function of adjudicating child labor violations"); *Withrow v. Larkin*, 421 U.S. 35, 58 (1975) (broadly affirming the consistency of agency adjudicative procedures with Due Process).

put through its paces. In the end, the government usually, though not always, wins, but administrative agencies usually win in the federal courts as well. *See* Zaring, *Reasonable Agencies*, *supra*, at 170.

Moreover, the SEC remains active in district court; currently, district court matters form a higher proportion of its enforcement docket than at any time in the past decade. To be sure, the SEC has brought some administrative actions in cases that are traditionally associated with civil enforcement in federal court, although this is not unprecedented. For example, 2014 featured twelve administrative proceedings brought for insider trading. SEC Fiscal 2014 Data at 3. But the SEC brought ten insider trading cases in the administrative forum in 2007, meaning that the defendants then would have been accountants, broker-dealers, investment advisors, or others registered with the commission. U.S. Sec. & Exch. Comm'n, *Select SEC and Market Data: Fiscal 2007*, at 3 (2007), https://www.sec.gov/files/secstats2007%2C0.pdf. Its use of the proceedings to hear foreign corrupt practices cases is new, although the number of such cases brought per year is in the single digits. SEC Fiscal 2014 Data at 3.

That said, as Urska Velikonja has found, "[b]y the second half of 2017, the SEC reverted completely, filing as few contested cases in administrative proceedings as it did in 2008 and 2009, well before the statutory change that sparked the controversy." Urska Velikonja, *Behind the Annual SEC Enforcement Report: 2017 and Beyond* 10 (2017), https://ssrn.com/abstract=3074073.

CONCLUSION

ALJs are not independent officers, but carry out the policies of the agency heads for whom they work. In addition to keeping routine matters off of court dockets, the SEC's ALJs offer defendants elaborate procedural protections, and conduct high quality proceedings that a quantitative and qualitative analysis shows is not biased toward the agency. For the foregoing reasons, the Court should not find that ALJs are officers of the United States within the meaning of the Appointments Clause.

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